HUD'S PROPOSED RESPA RULE

HEARING

BEFORE THE

SUBCOMMITTEE ON
OVERSIGHT AND INVESTIGATIONS

OF THE

COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

ONE HUNDRED TENTH CONGRESS

SECOND SESSION

SEPTEMBER 16, 2008

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HUD'S PROPOSED RESPA RULE

Tuesday, September 16, 2008

U.S. HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON OVERSIGHT
AND INVESTIGATIONS,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The subcommittee met, pursuant to notice, at 9:08 a.m., in room 2128, Rayburn House Office Building, Hon. Melvin Watt [chairman of the subcommittee] presiding.

Members present: Representatives Watt, Lynch, Cleaver, Green, Klein, Perlmutter; Miller and Royce.

Also present: Representatives Hinojosa, Manzullo, and Biggert.

Chairman WATT. This hearing of the Subcommittee on Oversight and Investigations of the Financial Services Committee will come to order. Without objection, all members' opening statements will be made a part of the record.

We will recognize as many members as wish to give an opening statement, within limits, for up to 5 minutes each, and I will recognize myself for a brief opening statement, just to set the stage.

Let me first welcome all of the witnesses; thank you for being here. As I explained to you before we got into formal session, these hearings normally start at 10 a.m., but there is a full Financial Services Committee markup this afternoon, and at the time we made the decision to move the hearing up to 9 a.m. to get out of the way of that markup, we actually had two panels of witnesses scheduled, which I will talk about. So I think members will be here. There is a substantial amount of interest in this subject, as reflected by the number of pieces of input that we have gotten in the process. But the 9 a.m. hour for Members of Congress is—at least for starting hearings as opposed to going to breakfasts and greeting constituents or doing the other parts of the job—a heavy lift.

Let me launch into a few comments. Today's hearing is entitled, "HUD's Proposed RESPA Rule." The Real Estate Settlement Procedures Act of 1974, which we call RESPA, is the Federal statute that governs the mortgage settlement process for all Americans. As anyone knows who has ever purchased a home or refinanced a home mortgage, the process involves most Americans' biggest investment and can be intimidating and complicated. Buyers and borrowers must sign dozens of forms and legal documents in one sitting, and quite often they do not understand everything they are signing. Sometimes they don't understand anything they are signing. RESPA mandates the disclosure of certain terms, such as a

home loan's initial interest rate, prepayment penalties, and settlement costs, among others.

RESPA and RESPA disclosures have been the subject of intense controversy and anticipated reform since at least the Reagan Administration. The Financial Services Committee has held several hearings on RESPA reform, most recently in the 105th and 108th Congresses. Our colleagues on the Small Business Committee have also held hearings on RESPA reform, most recently in May of this year. RESPA reform continues to generate bipartisan interest, and I thank Ranking Member Gary Miller for requesting this hearing, and we were happy to accommodate his request. It was at a bipartisan outcry and request that we pulled people together to discuss this.

The reason for today's hearing is to examine the proposed RESPA rule issued by HUD on March 14, 2008, for public comment. At the outset I should note that over 240 Members of Congress signed a "Dear Colleague" letter to HUD Secretary Steve Preston urging HUD to withdraw the proposed rule and commence a joint rulemaking with the Federal Reserve Board to produce more simplified mortgage and real estate settlement cost disclosure forms. The letter also warned that the proposed RESPA rule could hinder rather than help the recovery of the housing market, which is of even more concern in light of recent turbulence in the housing market and the government takeover of Fannie Mae and Freddie Mac.

Chairman Frank also wrote a letter to HUD Secretary Preston in June urging HUD to work with the Federal Reserve Board to reconcile inconsistencies between the proposed RESPA rule and the Truth in Lending Act, TILA, disclosure requirements to avoid consumer confusion and redundant disclosures.

I ask unanimous consent at this point that the Members' letter signed by over 240 Members of Congress to HUD, dated August 7, 2008, and Chairman Frank's letter, dated June 12, 2008, be made a part of the record. Without objection, it is so ordered.

I was one of the few Members of the House who was not a signatory to the letter of the over 240 Members, or to Chairman Frank's letter, and I may be the only remaining Member of Congress who can truly be said to be at least publicly neutral on HUD's proposal, so I was glad when Ranking Member Miller requested the hearing. I thought it would be fun to see a bipartisan pummeling of a Federal Government agency and a spirited defense by that agency. I am always up for a good fiery discussion, if not a brawl.

But, alas, that is not going to happen, at least not today, because before we could issue our invitation to HUD to come and explain what HUD was thinking, in August, HUD formally sent the proposed RESPA rule to the Office of Management and Budget for review and now claims that it is obliged not to comment further. So HUD Secretary Preston will not be with us today. That is why we only have one hearing panel today.

The Federal Reserve was not formally invited, but indicated that it would be reluctant to be critical of another Federal agency in public. I would note, however, that the Fed issued a staff comment letter, dated June 13, 2008, expressing some concerns, and I ask

unanimous consent to submit that letter for the record. Without objection, it is so ordered.

We are pleased that representatives of virtually every other group in America that I could think of have been lining up at the door to testify, which is why we have so many witnesses on this panel. We have a wide array of witnesses and we look forward to their testimony. The testimony will be available to HUD and to OMB for whatever use they desire to make of it as we move this process forward.

At the end of the day, RESPA reform should be about improving disclosure to consumers so that they can understand their rights and responsibilities when buying a home and avoid unwelcome surprises at the settlement table. While I have never been, and many of you have probably heard me express this view, a big advocate of the benefits claimed by the advocates of disclosure, it is certainly true that disclosure helps consumers better understand what they are signing when buying a home or getting a loan. RESPA reform should not unnecessarily confuse consumers, and should not result in unreasonable regulatory burdens and costs to the real estate industry as the fragile housing market seeks to recover.

I welcome the Members here. I am going to be as impartial as I can be today. I have fought to maintain this position, not signing on to any of the letters, and I was going to try to be the mediator. I am not sure there is going to be anybody here to mediate between, because having reviewed the statements, there seems to me to be pretty consistent opposition to the proposed rules for one reason or another.

I am looking forward to building this record, and I will recognize Ranking Member Gary Miller, who is actually the originator of the idea for this hearing, and we thank him for doing that. I recognize the gentleman for 5 minutes for his opening statement.

Mr. MILLER. Thank you, Mr. Chairman. It is good to have all of you here today. We are here today because of all of you.

Over the years, we have examined some of the RESPA proposals that have occurred in the past that haven't been enacted and we have all been very concerned. Many of you have come by the office and we have talked at different functions about your concerns, and I think it is most appropriate that we get those concerns out on the table. We really don't know what it is going to look like when we get the RESPA rule, but from what many are hearing, there are a lot of concerns. I will say that I have a lot of high regard for Secretary Preston. I think he is a good man, and he is going to try to do a good job, but I think it is also appropriate for us to talk.

Our industry, the mortgage industry, is going through incredible upheavals right now. We don't know how bad it is going to get, but we don't want to make it worse. What we don't want to do is, with our U.S. financial markets, experience the upheaval they have to make things more complicated. Record high foreclosures and delinquency rates, bank failures, and Treasury's recent actions with Fannie Mae and Freddie Mac, together with high commodity prices and the suffering labor market have truly put the U.S. economy to a test that we have never really experienced in recent years.

Certainly the foreclosure crisis has taught us all that we need to improve the mortgage origination process. Revamping these regula-

tions, however, must not be done haphazardly, especially considering the current housing market and the tightening credit situation. Our financial institutions are extremely vulnerable right now. We cannot afford any more large bank failures, and we need to focus on bringing stability to the housing and financial markets. Any reforms must not negatively impact mortgage affordability and availability in this extraordinary environment.

Furthermore, some housing experts are predicting that the mortgage losses will reach staggering levels in this coming year. While disclosures must be improved to prevent another mortgage crisis in the future, we must not exacerbate these losses, and we need to instill some certainty in the marketplace right now.

It is important for consumers to understand the terms of their mortgage. Comments of the Federal Reserve Board on HUD's proposal describe how the revised Good Faith Estimate, GFE, is inconsistent and duplicative of TILA's disclosure efforts which may lead to confusion or consumers disregarding crucial information about their loan terms. The Federal Reserve Board was extremely critical of HUD's proposal and warned that the lack of adequate consumer testing of these disclosures could ultimately hurt, rather than help, consumers, and I have talked to many of you and that seems to be your concern also. The Board also points out how HUD has failed to incorporate consumer testing results from their study in mortgage disclosure reforms.

The Federal Trade Commission, FTC, has also voiced concern with the proposed rule. The FTC has stated that some of the changes may further complicate the mortgage process. The FTC has also advocated a collaborative effort among HUD and the Federal Reserve Board to reform mortgage disclosures.

Additionally, 244 Members of Congress had concerns with the proposed rule and requested HUD to withdraw the rule and work with the Federal Reserve Board to reform mortgage disclosures. On August 18th, HUD rejected this request and sent the proposed rule to the Office of Management and Budget, OMB, on that very same day.

While we are unaware of the revisions that HUD made to the rule, it is important to have a discussion about the effects of the proposed changes. I look forward to listening to the concerns that you all are going to bring forward today, and hopefully HUD is listening at least on the TV to what we are going to do today. While we would have liked to have heard from HUD today about this extensive rule to reform mortgage disclosures, they declined our invitation to testify.

With that said, as many of you know, Secretary Preston previously served as an effective director of the Small Business Administration. Mr. Preston made important reforms to the Administration and understands the needs of America's entrepreneurs, lenders, and small businesses. I believe the Secretary brings great experience to the Department of Housing and Urban Development, and I am confident that he is taking this issue and your comments seriously with his great consideration of reforming the mortgage lending process.

You are an incredibly talented bunch of witnesses that we have today, you understand your industry and your market, and I am

really looking forward to the testimony. I thank you for holding this hearing, Mr. Chairman.

Chairman WATT. Thank you for requesting the hearing, and I thank you for your opening statement.

I am going to go a little bit out of order because I know Mr. Cleaver and Mr. Green have to leave for a meeting that I also need to be at but I can't attend, so they are going to be my eyes and ears at that meeting. So Mr. Cleaver is recognized for 5 minutes.

Mr. CLEAVER. Thank you, Mr. Chairman. I won't take 5 minutes.

I would like to express my appreciation to you and Ranking Member Miller for holding this hearing. I am very sorry that the Department of Housing and Urban Development did not send a representative here today and also submit to the questions that we might ask.

The proposal is a very sensitive issue, and the chairman and others have already expressed their opinions. And to be quite frank, I know people don't normally like to have group projects. People don't like to work together or come together, but I can't come up with any logical reason why there cannot be collaboration between HUD and the Fed. It is just not practical to say that we can't come to a hearing because Federal agencies don't like to contradict one another. Their very existence in many instances is a contradiction to other agencies.

And so I am very interested in hopefully getting back to hear your answers to questions. Ms. Borne articulated in her statement some things that I really would like to get into. I appreciate the fact of your coming, and I can hope that with all of the various witnesses we have today that somehow we can get HUD to consider some of the conclusions and suggestions that many of you have reached and I think, frankly, many of us have already reached. So I look forward to getting back in time to listen to some of your comments or to listen to the answers to some of the questions we raise.

Thank you, Mr. Chairman.

Chairman WATT. Mr. Miller is recognized for a unanimous consent request.

Mr. MILLER. Yes, Mr. Chairman. I would like to submit the letter from HUD into the record regarding their not testifying today. And I really wish they could have been here, at least to testify on what the original RESPA proposal was. We could at least have had some questions answered on that. Nevertheless, I ask to submit this letter for the record.

Chairman WATT. Without objection, the letter will be made a part of the record.

Now lest you all be concerned that I am going to pass over Mr. Manzullo, he is not on the subcommittee, and I am going to personally ask, along with Mr. Miller, that we give him unanimous consent to make an opening statement, but I need to let the members of the subcommittee make their opening statements first. So I will go next to Mr. Green for up to 5 minutes.

Mr. GREEN. Thank you, Mr. Chairman. I especially thank you for holding this hearing, and I thank Ranking Member Miller as well. He has demonstrated a willingness to work with us across the aisle in a bipartisan fashion and I appreciate what he has done to work with me on some other issues.

Mr. Chairman, as Ranking Member Miller indicated, we don't know what the reform will look like, and I concur. But I also do know this: We must act. Even when we do act, there are those who contend that we haven't acted. I think that the least we can do is make sure that we can have a reasonable retort to those who will contend that we have not done anything and show that we have done something of worth. We understand that knowledge is power, and what we must do is empower the consumer by according the consumer the knowledge necessary to make reasonable, prudent, and judicious decisions.

We have some concerns that I think can be addressed. We have two agencies that are charged with the responsibility of dealing with these issues. The Truth in Lending Act directs the Federal Reserve Board to regulate disclosures on loan terms. RESPA directs HUD to do so. These two entities may not harmonize all the time, and as a result we may not get harmony in terms of what should be accorded the consumer with the disclosure forms.

I am concerned about the yield spread premium. The yield spread premium has caused many persons to pay fees that they ordinarily would not have paid had they known they were being accorded these fees. These fees were being placed upon them. There must be some way for the consumer to make an intelligent decision about the yield spread premium. For those who do not know who may be viewing this, the yield spread premium is a fee that an originator can get when he or she causes a borrower to take out a loan for an interest rate higher than the one the borrower has qualified for, and it need not be disclosed to the borrower that this fee is being charged. The yield spread premium is a concern. We have to have fairness in borrowing such that people know what they are confronting.

The initial rate versus the adjusted rate is a concern. Many consumers don't understand this whole notion of a teaser rate and then a rate that will adjust that they cannot pay for. The adjusted rate has to be made clear to consumers. The prepayment penalties—there are many consumers who don't know that they have prepayment penalties when they take out their loans. This is something that we have to make available and known to consumers.

And finally, just the cost of the loan. And by the way, I say finally only because I think my time doesn't permit me to go into a multiplicity of other things. But the cost of the loan, there are many consumers who literally, at the time they negotiate their loan, have no idea as to what this loan will cost them. Why? Because consumers are so eager to have a place to call home, especially the first-time homebuyer, that they will sign anything. They literally sign documents that have no language on them, and they are told, "We will get this back to you at a later time," and they then contend, "I didn't sign that with that on it," at the later time and find that is not going to be justification for having signed the document and the liabilities associated with the document.

So I am very concerned about the consumer. I want the consumer to be empowered with knowledge. We can do this, but I do think that it is going to require bipartisanship, and I think that it is going to require that we have the opportunity to talk to HUD and to the Fed about this.

I thank you and I yield back the balance of my time.

Chairman WATT. I thank the gentleman for his participation. Mr. Lynch is recognized for 5 minutes.

Mr. LYNCH. Thank you, Mr. Chairman, and I want to thank Ranking Member Miller as well. I will try to be very brief; I do want to hear from our witnesses this morning.

I want to thank all of the panelists here for attending. I would be remiss if I didn't express my disappointment with HUD and with the Fed for their failure to attend. I simply cannot imagine how this helps the American people have any confidence in the fact that our agencies are working with government to address the problems that they face in these extraordinary times when these agencies don't even show up. While I understand the difficulties there, there should have been some way to send someone here to address the points that the committee and that you on the panel are raising.

With that, I just want to point out, I know that, Mr. Savitt, your organization (the National Association of Mortgage Brokers) and Mr. Kittle, your organization (the Mortgage Bankers Association) are intimately involved in the current difficulties that we are facing, not only on the subprime but generally. I will be very keen to hear what you might think we can do to improve the settlement process. And I know that many of the frailties and weaknesses that we see in the mortgage origination process come from the underwriting side, perhaps, but I do think that the moment of settlement is a time at which some of these weaknesses could be brought to light and the underlying agreements strengthened.

So I will be interested in hearing from you, but also from everyone who has come here this morning to help Congress with its work. So thank you, Mr. Chairman, and I yield back.

Chairman WATT. I thank the gentleman for his comments.

And I join Mr. Miller in asking unanimous consent for permission to allow Mr. Manzullo to give an opening statement. I know he has been active on this issue in the Small Business Committee, so we welcome his opening statement. The gentleman is recognized.

Mr. MANZULLO. Thank you, Mr. Chairman, for holding this hearing today and for allowing me to testify.

I have been a longtime opponent of changes to RESPA. During my time as chairman of the Small Business Committee, I held two hearings on the impact of HUD's proposed RESPA changes on small businesses. At both hearings, I was strongly dissatisfied by the lack of knowledge displayed by HUD staff regarding the details of their own proposal and the impact that it would have on consumers and businesses. Secretary Jackson testified that there are eight people working full time at that Department just on the RESPA issue. Their time could be well spent doing something else, such as trying to figure out what to do with this horrible real estate market.

In June of this year, I sent a strongly worded comment letter to HUD emphasizing that they have again displayed a serious lack of familiarity with real work experience in the real estate settlement process. I have been involved in over 2,000 real estate closings as a member of the bar for 22 years before I was elected to Congress, and I can tell you they have no clue as to what happens at a real

estate closing, and now they come here with this, again, ridiculous regulation that could really hurt. I recently met with HUD's Secretary Preston, a man I hold in high regard, to discuss these changes.

Although I see many problems with the current RESPA proposal, I want to mention just a couple of them. First of all, HUD has never complied with the Regulatory Flexibility Act. I repeat, HUD has never complied with the Regulatory Flexibility Act. Never. The data used here is 6 to 8 years old. It was incomplete back then, it is incomplete now, and they ought to hang their heads in shame over lack of scholarship and come out with the impacts that this has on small business. And they come back again, and again, and again with the same old crap. I just cannot believe that regulators have nothing else to do but to sit there and destroy small businesses. And now it comes back again, the bungling of services to help out big people and destroy the small businesses under the veiled name of the "volume discount."

HUD ought to do what its statutory duty is to do. Before RESPA came out, I closed real estate transactions with a one-page form, and everybody knew exactly what the cost of that mortgage was, exactly all of the different costs. Today, more confusion. I would just ask HUD, just withdraw this thing. Just throw it into the river and get on with something else in your lives. I guess you know where I stand, Mr. Chairman.

Chairman WATT. I thank the gentleman for his comments, and now we have ourselves fired up here.

I welcome the gentlelady, Mrs. Biggert, to the hearing. She is not a member of the subcommittee either, but I ask unanimous consent to allow her an opening statement if she desires to make one.

Mrs. BIGGERT. Thank you, Mr. Chairman. I don't have an opening statement, but I would like to submit for the record a letter that Congressman Ruben Hinojosa and I submitted to OMB about the HUD RESPA and asking them to send it back to HUD and to have further hearings on such a ruling that they have made.

Chairman WATT. I thank the gentlelady for her unanimous consent request, but we have already submitted that letter. That is the one that was co-signed by about 240 Members, as I recall, or is there another letter?

Mrs. BIGGERT. Yes, sir.

Chairman WATT. There is a separate letter? Okay.

Mrs. BIGGERT. This is a further letter that was submitted yesterday, and we are getting signatures, again, on this letter.

Chairman WATT. Without objection, that letter will also be submitted for the record.

I think we have exhausted all of the opening statements now. I told you that there was a great deal of interest in this, and there will be other members coming in, I am sure, probably after 10:00. There is a conference going on, a Republican conference, and some meetings that I am aware of, so it is a busy day.

So let's get to the witnesses. Without objection, all other members' opening statements will be made a part of the record. I will now introduce briefly the members of the panel who will be testifying today. Your full bios and CVs will be made a part of the record, so we are going to abbreviate the introductions.

We welcome you here. Our first witness will be Mr. Mark Savitt, president of the National Association of Mortgage Brokers.

Our second witness will be Mr. David Kittle, president of the Mortgage Bankers Association.

Our third witness will be my homeboy, T. Anthony Lindsey from Charlotte, who is here representing the National Association of Realtors, and he is also the chief executive officer of GlobeCrossing, LLC, a diverse real estate company in Charlotte, my hometown.

Our fourth witness will be Ms. Margot Saunders, counsel for the National Consumer Law Center, with whom I have also had a long and warm relationship, going back to North Carolina.

Our fifth witness will be Ms. Rebecca Borne, policy counsel for the Center for Responsible Lending.

Our sixth witness will be Mr. Gary Kermott, president—did I get that right? Kermott? Somewhere in the neighborhood, he says—president of the American Land Title Association.

Our next witness after him will be Ms. Debra Still, president and chief operating officer of Pulte Management, LLC, and she is speaking on behalf of the National Association of Homebuilders.

And our final witness today will be Mr. David Stevens, president, Affiliated Businesses, Long and Foster Companies, on behalf of Real Estate Services Providers Council (RESPRO), our most recent addition to this panel.

Mr. MILLER. Pulte Mortgage. It is supposed to be Pulte Mortgage, LLC.

Chairman WATT. Pulte Mortgage, LLC. I am sorry. Just trying to rush through this.

So we welcome all of you. Your written statements that you have submitted will be made a part of the record in their entirety, and each of you will be recognized for 5 minutes to summarize your statement and highlight some of the points that you wish to make. There is a lighting system in front of you. It will come on green at the beginning. At 4 minutes, it will go to yellow, and at 5 minutes, it will go to red. We are not in the habit of being as mean as some Chairs are, but we do ask you to respect that there is another demand for this room, and so we ask you to kind of sum up when you get to that red light before we have to ask you to do that.

So Mr. Savitt, you are recognized for 5 minutes for your statement.

STATEMENT OF MARC S. SAVITT, PRESIDENT, NATIONAL ASSOCIATION OF MORTGAGE BROKERS (NAMB)

Mr. SAVITT. Good morning, Chairman Watt, Ranking Member Miller, and members of the subcommittee.

I am Marc Savitt, president of the National Association of Mortgage Brokers. In addition to serving as NAMB president, I am also a licensed mortgage broker, and like most of my fellow NAMB members, I am a small business owner.

I would like to thank you for the opportunity to testify here today on HUD's proposed RESPA rule. NAMB applauds HUD's response to the current problems in our mortgage markets. We share HUD's resolute commitment to simplify the process of obtaining mortgages and to protect consumers from unnecessarily high settlement costs.

However, NAMB objects to several elements of the proposal that would not best serve consumers because they would confuse consumers, impede competition, and treat direct competitors differently. In addition, HUD has failed to consider other highly effective and less burdensome alternatives to their proposal. In light of the current mortgage situation, in addition to recent rulemaking and the passage of key legislation, NAMB questions the appropriateness of the timing and implementation of HUD's proposal.

A significant component of the proposal addresses broker compensation or YSP. YSP is already required to be disclosed on the good faith estimate and on the HUD–1 settlement statement for the last 16 years since 1992. The proposal, however, reclassifies this compensation as a credit to the borrower, the practical effect of which will be very confusing to consumers and puts brokers at a competitive disadvantage by imposing uneven disclosure obligations among originators receiving comparable compensation. YSP or its equivalent is present in every origination channel regardless of whether a broker is involved in the transaction or not. In fact, with the originate to distribute model, most originators are merely brokering loans, yet HUD fails to address the converging roles of mortgage originators in its proposal.

HUD's proposal addresses broker disclosure in an inequitable manner and in a way that will confuse consumers about the overall cost of a mortgage. This is not simplifying the mortgage process. There needs to be a level playing field for consumers.

The proposal relies on testing that was conducted using flawed methodology to assess the value of HUD's proposed disclosures relating to YSP. Additionally, HUD failed to test the disclosures in actual transactions involving competing originators, thereby producing flawed results. Exhaustive studies of mortgage disclosures as detailed in our written testimony issued by the FTC, the Federal Reserve Board, and academic scholars show that broker-only disclosure of YSP creates confusion among consumers and causes them to choose more expensive loans. Additionally, these studies show that broker-only disclosure of YSP leads to bias against broker-assisted transactions and impedes competition, resulting in harm to consumers.

Such authoritative research and studies, in addition to consumer testing, led the Federal Reserve to remove broker-only disclosure provisions from its final rule amending Regulation Z of the Truth in Lending Act. NAMB has urged HUD to take a similar action with regards to its proposal and we encourage HUD to work with the Fed to produce an alternative disclosure proposal.

One alternative NAMB strongly supports is a revised GFE that clearly outlines loan terms and the originators role in the transaction. NAMB has submitted the prototype of such a form to HUD on several occasions. However, HUD has yet to comment on this proposal.

Finally, NAMB opposes the section of the proposal that would require an addendum to the HUD–1 settlement statement which would compare loan terms and settlement charges estimated on the good faith to the HUD. Because the addendum, or closing script, as it is known, is required to be read out loud by the settlement agent in closing, it will unnecessarily complicate the settlement

process, delay closings, and ultimately drive up costs to the consumers.

Our mortgage market today is significantly strained, and it continues to experience ongoing turmoil and change. Because of this, NAMB believes that consumers and the market in general may be better served if HUD would consider delaying implementation of any new policies or procedures until the market and all market participants have had time to digest the multitude of events already affecting consumers' ability to obtain credit. We also would like to see HUD harmonize its RESPA rule with the Fed's implementation of Reg Z.

We look forward to continuing to work with this subcommittee as well as with HUD and other regulators on finding solutions that are effective in helping consumers but will not unreasonably obstruct the market or disadvantage competing originators. I thank the committee for allowing me to testify today, and I would be happy to answer any questions.

And Mr. Chairman, I would like to make one other statement if I could. Mr. Green made a comment in his opening statement that YSP was not disclosed to consumers, that they basically found this out when they got to closing. YSP, which is disclosed by mortgage brokers, were the only channel of distribution that actually discloses in this indirect compensation. We have been doing this since 1992 on the good faith estimate when the consumer first comes into our office, and once again at the settlement on the closing statement, and most States, such as the States in which I am licensed, also required two State-specific forms. So when a consumer comes into my office, I disclose it 4 times.

Thank you.

[The prepared statement of Mr. Savitt can be found on page 259 of the appendix.]

Chairman WATT. I thank the gentleman for his testimony, and Mr. Kittle is recognized for 5 minutes.

STATEMENT OF DAVID KITTLE, PRESIDENT, MORTGAGE BANKERS ASSOCIATION (MBA)

Mr. KITTLE. Chairman Watt, and Ranking Member Miller, thank you for the opportunity to appear before you to discuss RESPA, one of the Mortgage Banker Association's top policy issues.

I would like to make three points, and then I would be happy to answer any questions. First, MBA and I, personally, are firmly committed to improving the mortgage process for both industry and consumers, and we have been for a very long time. Second, any reforms should give consumers the information they need to effectively shop for loans, to inform themselves about the true cost of closing on a mortgage, and to protect themselves from unscrupulous actors in the mortgage process. That requires a comprehensive approach to the loan application and closing process involving both HUD's RESPA reforms as well as the Federal Reserve's TILA forms. And last, HUD's proposed RESPA reforms do not even come close to achieving simplification. They should be delayed and officials at HUD should work with the Federal Reserve on a joint and comprehensive effort to simplify and improve forms and disclosures.

Improving the mortgage closing and application process will result in better informed customers who understand their loans and the closing process. With greater transparency and better information, consumers can shop more effectively. This will lead to better mortgage decisions, and those lenders who can objectively provide the best products for their customers will be the companies that get the most business. The market will become more efficient. Lenders will have better and happier customers.

Reform is right for the market and for consumers. But reform for reforms sake would be quite damaging to the system. Reforms should achieve two interrelated goals: One, help the consumer shop; and two, help them understand their loan and the closing terms better. That is why it is imperative that HUD not work in isolation on this issue, but work with the Federal Reserve in helping consumers shop for and understand their loan.

The Fed is responsible for implementing the Truth in Lending Act, or TILA. HUD is responsible for RESPA. At the time of the application, borrowers receive a TILA disclosure and a good faith estimate of closing costs. In the middle of the process, recently passed Federal law now mandates another TILA disclosure. Then, at the closing table, the borrower gets yet another document, the HUD–1, which is different from the previous two documents.

All of these documents are ultimately confusing for the consumer. You simply can't compare one document to another without a map. It is so confusing, HUD literally has created a map between the two documents. How is that simplification? Real simplification would look at all of the documents and harmonize them so they can work together. Incredibly, this HUD RESPA proposal would make actual forms less similar. This is exactly what consumers do not need. If you have purchased a home, you have some idea how the closing process works. Does anybody really believe that the way to fix the closing mess is to make a closing longer and to give more paper to consumers?

What HUD has proposed would take what should be a one page form and turn it into four pages, require a 45-minute script to be read to the consumer, stretching an already long closing process with no benefit to the borrower, and continue to have a series of forms where the lines don't match up and consumers can't figure out what happens from one part of the process to the next.

MBA has long supported efforts to make the mortgage process simpler, clearer, and more transparent for consumers. Common sense dictates that HUD and the Fed work together. The rules and forms should be harmonious, work for borrowers, and be implemented at the same time to avoid confusion and unnecessary costs for lenders, sellers, and buyers.

In closing, let me say that we all know that the context of this hearing is the larger situation in the mortgage and financial markets. As you know, right now the market is fragile. This is not the time to ask the industry or consumers to assume costs of regulatory changes unless they are necessary and well-conceived. We need reform, but we have to make sure we get the right reform. We are pleased that HUD attempted to make a very difficult task. They deserve to be commended for their efforts, but unfortunately HUD's efforts will not give consumers what they need.

Again, I thank you for the opportunity to appear before you, and I look forward to answering your questions.

[The prepared statement of Mr. Kittle can be found on page 94 of the appendix]

Chairman WATT. I thank the gentleman for his testimony, and we will now go to Mr. Anthony Lindsey on behalf of the National Association of Realtors.

STATEMENT OF T. ANTHONY LINDSEY, CHIEF EXECUTIVE OFFICER, GLOBECROSSING, LLC, ON BEHALF OF THE NATIONAL ASSOCIATION OF REALTORS (NAR)

Mr. LINDSEY. Good morning, Chairman Watt, Ranking Member Miller, and members of the subcommittee.

Thank you for holding this hearing and for giving me the opportunity to share the concerns of the National Association of Realtors and its 1.2 million members with the proposed rule to reform the Real Estate Settlement Procedures Act, known as RESPA. Again, my name is T. Anthony Lindsey. I am the founder and chief executive officer of GlobeCrossing Realty in Charlotte, North Carolina. I currently serve as a director on the board of the North Carolina Association of Realtors and a director on the board of governors for the Real Estate and Building Industry Coalition, which serves the metro region of Charlotte, North Carolina. In addition, I owned and operated a regional residential mortgage brokerage for 6 years.

Reform of RESPA is critically important to NAR members simply because it affects almost every home purchase. Since many consumers look to the real estate professional to help them understand the home buying process, the consumer turns to us when they have questions. We clearly recognize the need to reform RESPA and make the process easier to understand.

However, we believe that HUD's current RESPA reform proposal falls short of this stated goal. Specifically, we believe that the new good faith estimate and anti-competitive aspects of the rule need further revision. NAR believes the new rule does not simplify the transaction or provide full disclosure. In fact, it will most likely cause confusion, reduce the incentive to shop, and likely raise prices for settlement services in the long run. For example, going from a two page GFE to a four page GFE does not achieve simplification in our view.

The new good faith estimate should mirror the HUD–1 settlement statement, as was suggested by HUD's own design consultants. Marrying these two forms would help consumers understand whether the terms and expenses that were disclosed to them upon loan application are in fact the same ones outlined at closing. Despite its longer length, the new GFE does not include all closing costs, another factor that will contribute to misunderstanding and probably inhibit shopping. NAR, along with the Center for Responsible Lending, has recommended that HUD develop a one page summary GFE for shopping purposes and a full GFE matched to the HUD–1 statement that includes all closing costs to help reduce this confusion. We also believe that HUD and the Federal Reserve should coordinate their efforts to revise the RESPA disclosure forms and the Truth in Lending rules as called for by Congress some 12 years ago.

HUD must also consider the anti-competitive consequences of the good faith estimate. As proposed, the good faith estimate carries a HUD required price guarantee only for a lender-provided package of settlement services. As a result, we believe consumers will be less likely to shop for these services, especially when it is pointed out to them that a second GFE would be required if they do shop and there might be a charge for the second GFE. This point is very important and one that gets little attention in the RESPA debate. The largest financial institutions will likely benefit the most from these new pricing provisions. We anticipate they will use their market clout and promises of high volume business to force down prices so they present the lowest cost packages of services and capture market share.

Now on the face of it, that sounds good, and we support the goal of lower cost, but we and many others believe that reduction in prices will only be temporary. In the long run, closing costs will rise and service quality may diminish as smaller lenders and local settlement firms are pushed out of the market.

In conclusion, NAR strongly supports better disclosures of mortgage terms and settlement services. HUD's RESPA reform proposal, however, should be reworked to focus on common sense disclosures while eliminating the volume discount, the closing script, and—provisions.

Thank you very much, and I will be happy to address any questions.

[The prepared statement of Mr. Lindsey can be found on page 203 of the appendix.]

Chairman WATT. I thank you very much for your testimony.

Ms. Margot Saunders of the National Consumer Law Center is recognized for 5 minutes.

STATEMENT OF MARGOT SAUNDERS, COUNSEL, NATIONAL CONSUMER LAW CENTER (NCLC)

Ms. SAUNDERS. Thank you, Chairman Watt, Mr. Miller, and members of the subcommittee. We appreciate the opportunity to speak today on behalf of low-income consumers.

The National Consumer Law Center works with lawyers all over the country, legal services, and private lawyers who try to help clients to prevent them from losing their homes. I see hundreds of mortgages every year, and there is no doubt that the current system is broken. RESPA does need reform. We think that HUD's latest proposal is a good way down the road towards positive reform of RESPA. We agree with the members of this panel, however, that more work needs to be done. We hope that the current effort is not suspended, but instead that HUD continues to improve the regulations, as recommended, and then finalize them. In our lengthy comments to HUD as well as our testimony we have provided comprehensive responses to all of the myriad of issues that HUD raises.

In the few minutes that I have today I want to focus on just two of those issues. One, the necessity to include the APR, the annual percentage rate, rather than the interest rate in the good faith estimate, and two, the dangers of the proposal on yield spread premiums.

HUD is appropriately focused on reducing costs for consumers and facilitating shopping. The APR in the mortgage market is a necessity to achieve those goals. It is the only shopping metric that allows consumers to equate all fees, all potential interest rates, over the full term of the loan. We know from research that most consumers do use the APR when they are shopping for mortgages. Interest rates, while reflecting the largest cost of credit, do not reflect other important aspects of credit.

In recent years, the marking of dangerous payment option ARMs reveals the problem with relying too much on interest rates. The payment option ARMs are typically advertised, for example, as a 2 percent fixed rate, even though the rate may be fixed for no more than a day or a month. The APR, while it does not entirely reflect the upwards adjustment in the interest, at least reduces the distortion by requiring that the rate be disclosed as a composite rate over the term of the loan. Consumers cannot do the math to determine which of two loans is cheaper given different rates, different fees, and different terms. The APR solves that problem and permits consumers to shop intelligently and efficiently.

Yield spread premiums must be substantively regulated. Lender-paid broker compensation, as HUD describes, leads to higher settlement costs and higher interest costs. Generally, borrowers receive little if any benefit from lender-paid broker compensation. Worse, lender-paid broker compensation appears to drive racially disparate pricing. Only where the fees are either all in or all out of the rate are consumers able to shop successfully for the cheapest loan.

When consumers can compare loans with the fees all in or all out, they are comparing a limited number of variables. On the one hand is a loan with a particular rate and all fees required to be paid by the borrower either in cash or out of the home equity of their loan. On the other hand is the same loan with all of the fees paid by the lender but from the interest rate, no additional cash or equity is required. This is a no-cost loan.

There are multiple benefits for no-cost loans, including the retention of precious cash and equity, as well as the lesser known finding that no-cost loans result in significant reduction of all closing costs. However, the key to achieving this reduction is that the lender has to pay all the fees; there cannot be a mix. The use of the combination of payments has the opposite effect and the studies routinely find that the combinations of payments result in a higher total of closing costs.

Most disclosures of lender-paid broker compensations are likely to confuse consumers because the trade-offs are so complex and because borrowers are led to believe erroneously that brokers are acting as their agents. We share HUD's concerns that a separate agreement is likely to confuse borrowers. We agree that the impact of any permissible yield spread premium must be clearly disclosed on the GFE. However, HUD's use of the term "credit" to describe lender-paid broker compensation in the absence of substantive regulation that limits total fees is terribly misleading.

The key point is that disclosure of a loan is not sufficient. Yield spread premiums should be prohibited unless all other fees are folded into the interest rate and no discount points are charged.

Additionally, no other lender-paid broker compensation should be permitted if the borrower is making any direct payments to the broker.

Thank you. I will be happy to answer any questions.

[The prepared statement of Ms. Saunders can be found on page 233 of the appendix.]

Chairman WATT. Thank you so much for your testimony.

Ms. Rebecca Borne, on behalf of the Center for Responsible Lending, is recognized for 5 minutes.

STATEMENT OF REBECCA BORNE, POLICY COUNSEL, CENTER FOR RESPONSIBLE LENDING

Ms. BORNE. Good morning, Chairman Watt, Ranking Member Miller, and members of the subcommittee. Thank you for inviting me to testify today about RESPA. I am policy counsel at the Center for Responsible Lending, a not-for-profit nonpartisan research and policy organization dedicated to protecting homeownership and family wealth. We are an affiliate of Self-Help, a lender that makes responsible fixed-rate mortgage loans to people with blemished or nontraditional credit. We first wish to congratulate HUD for its efforts to improve RESPA. Confusing and misleading information has contributed to this foreclosure crisis.

However, we cannot overemphasize that poor disclosure has not been the driver of this crisis and that improving disclosure will not prevent future predatory lending. This crisis was primarily caused by lenders and brokers selling unsustainable loans, largely in response to secondary market demand. Only substantive laws will prevent predatory practices, realign incentives, and ultimately restore health to the mortgage market. HUD, through RESPA, has the authority to eliminate one of the key culprits of the subprime crisis, abusive yield spread premiums.

In designing RESPA, Congress adopted not only disclosure provisions, but also substantive ones aimed to prevent anti-competitive conduct that makes mortgages unnecessarily more expensive. As has already been noted today, yield spread premiums, or YSPs, are payments from lenders to brokers in exchange for the broker selling the borrower a loan with a higher interest rate than the borrower qualifies for. RESPA has long prohibited payments for simply delivering a loan with a higher interest rate, calling these kickbacks. HUD has said, though, that since consumers can use YSPs to buy down upfront origination costs, they deliver value and are not prohibited.

But in reality, particularly in the subprime market, this tradeoff of rate and upfront costs rarely, if ever, occurred. Consumers unknowingly paid YSPs and earned no corresponding reduction in upfront costs. The single most effective action HUD could take to protect consumers through RESPA is to refine its policy position to allow YSPs only when they result in a corresponding reduction in upfront costs. This would help reform the subprime market without significantly impacting the prime market.

In its proposed rule, HUD attempted to address YSPs through its origination cost disclosure on the good faith estimate. However, the disclosure will not ensure a price tradeoff between YSPs and upfront costs. This shortcoming does not represent a failure on the

part of the disclosure as much as it reflects the impossibility of ensuring a price tradeoff without substantive reform. If we are going to try to rely on disclosure alone, the proposed disclosure should be much improved.

We understand that in designing the disclosure, HUD attempted to treat lenders and brokers evenhandedly. However, we don't think HUD should do so at the expense of a more comprehensible disclosure that better alerts consumers to the risky nature of YSPs, especially considering that our most recent research shows that borrowers pay significantly more for subprime loans originated by independent brokers versus retail lenders. HUD's own recent study of FHA loans was consistent with our findings. Our testimony and our comments to HUD on the proposed rule include several specific recommended improvements to the origination cost disclosure.

With respect to GFE provisions more generally, HUD and the Federal Reserve should coordinate to develop one integrated disclosure form. Short of this, we have made several recommendations for how HUD should improve its GFE so that it better alerts consumers to the riskiest features of their loans. Critically, HUD should require that terms be binding for 30 days instead of 10, and it must provide an interest rate lock of at least 10 days to prevent common bait and switch tactics.

Finally, we strongly support HUD's request that Congress enhance RESPA's civil penalties and equitable relief. We further request that Congress add a private right of action for all elements of RESPA, especially the GFE and the HUD–1. The lack of a private right of action has meant that abuse often carries no consequences, in which case even the most perfectly designed disclosure will not help consumers. Thank you again for this opportunity to testify today, and I look forward to your questions.

[The prepared statement of Ms. Borne can be found on page 49 of the appendix.]

Chairman WATT. Thank you for your testimony, Ms. Borne.

Mr. Gary Kermott, president of the American Land Title Association, is recognized for 5 minutes.

STATEMENT OF GARY KERMOTT, PRESIDENT, AMERICAN LAND TITLE ASSOCIATION (ALTA)

Mr. KERMOTT. Thank you, Chairman Watt, Ranking Member Miller, and members of the subcommittee. Thank you for the opportunity to testify on HUD's proposal to amend RESPA. I would also like to thank Representatives Hinojosa and Biggert and all the members who signed the Dear Colleague letter that was sent to HUD.

As the 2008 president of the American Land Title Association, I am speaking on behalf of our 3,000 title insurance companies, agents, abstractors, escrow officers, and attorneys who search, examine, insure land titles, and perform real estate closings. A majority of our members are small businesses with fewer than 20 employees.

As we are all painfully aware, the real estate market is experiencing a downturn of historic proportions. The recent Federal takeover of Fannie Mae and Freddie Mac, and the bankruptcy filing yesterday of Lehman Brothers are just the latest examples of the

severe stress in the housing and financial markets. Although we all agree with the goal of increasing transparency and simplifying the transactions, HUD's rule does not do so. It would add increased new regulatory burdens on the industry and confusing, lengthy disclosures to homebuyers. In the current environment, it would make things worse.

My remarks today will focus on four areas of the rule that would be most harmful for our members and homebuyers. First, the closing script. The closing script should be eliminated from the rule. Why? First of all, it is too late at the closing for a homebuyer to change the terms of the loan. In some cases, the moving van is parked outside. Second, the settlement agent doesn't have the information or knowledge to answer questions raised by the closing script. Third, the increased costs for longer closings will fall on the homebuyers. And finally, in some States, it would violate unauthorized practice of law statutes. Another point that HUD fails to recognize is that over 50 percent of closings occur at the end of the month. The increased time to draft, read, and explain the closing script will harm smaller settlement companies because they lack the resources to add personnel and physical space to accommodate these extended closings.

Second, title and closing fee disclosures. The disclosure of title and closing fees on the proposed forms is misleading and will discourage shopping by homebuyers for the services that are in their best interests. Why? Because the new GFE only discloses an aggregate figure for a range of services. That makes it more difficult for the consumer to shop for individual services at a lower price. They won't know what is in the so-called package. Similarly, by lumping together so many different charges into the category of primary title services on the new HUD–1, the buyer and seller will not know how their funds were actually dispersed and to which providers. This defeats a primary purpose of the HUD–1 as a record of the transaction. This will also hide what fees the seller may have negotiated or be required to pay under State law, practice, or contract. Title and closing fees should all be itemized on both the GFE and the HUD–1 to encourage shopping.

Third, volume discounts and tolerances. As proposed by HUD, the allowance of volume discounts will be impractical, anti-competitive, and will harm small title insurance companies, small banks, mortgage brokers, appraisers, and other small settlement businesses. It is in fact a disguised form of packaging that was uniformly rejected in 2002. The largest companies have the resources to either favor their own affiliated companies or to create a network of preferred providers that can offer services at or below cost. This will push small independent providers out of business, resulting over time in less competition and higher prices. Our members do not believe that HUD should dictate such changes. The tolerance provisions will inhibit shopping. The message from the lender to the borrower will be, "Go with my recommendations, you will get a better deal." Yet there is no guarantee that these recommended service providers are the least expensive or the best. Again, this will discourage shopping.

Finally, the proposed forms are confusing. They create more problems for the homebuyer than they solve. They are very con-

fusing. For example, as has been mentioned by my panel colleagues, the proposed GFE would differ from TILA in its treatment of interest rates. Also, by characterizing the yield spread premium as a credit to homebuyers will be very, very confusing.

In conclusion, ALTA recommends that HUD limit its efforts to simplifying only the GFE and the HUD–1 so that comparisons can be easily made between the documents. ALTA, along with the National Association of Realtors and the Center for Responsible Lending have worked together to develop new GFE and HUD–1 forms that are clearer and more transparent than both the existing and the proposed HUD forms. This would be a huge improvement for homebuyers without imposing an extraordinary cost on our small business members.

Thank you.

[The prepared statement of Mr. Kermott can be found on page 66 of the appendix.]

Chairman WATT. Thank you for your testimony. I will try to get it right this time. Ms. Debra Still, president and chief operating officer of Pulte Mortgage LLC, on behalf of the National Association of Homebuilders, you are recognized for 5 minutes.

STATEMENT OF DEBRA STILL, PRESIDENT AND CHIEF OPERATING OFFICER, PULTE MORTGAGE LLC, ON BEHALF OF THE NATIONAL ASSOCIATION OF HOMEBUILDERS (NAHB)

Ms. STILL. Thank you very much. Chairman Watt, Ranking Member Miller, and members of the subcommittee, on behalf of the 235,000 members of the National Association of Homebuilders, thank you for holding this hearing and for the opportunity to share our concerns regarding HUD's proposed RESPA changes.

My name is Debra Still. I am president and CEO of Pulte Mortgage, a subsidiary of Pulte Homes, one of the Nation's largest homebuilders with operations in 26 States. My comments today focus on HUD's proposed definition of required use, which would prohibit a homebuilder from offering incentives in exchange for a buyer's use of the affiliated mortgage or title company. Our position is that HUD's proposed definition would have an immediate negative impact on the efficient operations of homebuilders and the majority of consumers buying new homes and that HUD has not established a sound rationale for this change.

Most homebuyers need a loan to buy a home and this financing is a critical part of the home buying process. Homebuilders create affiliates to ensure that the financing is ready when the home is complete and to enhance the customer's overall home buying experience. Any home that fails to close on time hurts the builder in the form of financial and reputational costs and creates a hardship for the buyer. With aligned processes, affiliates consistently outperform outside lenders in executing timely closings because outside firms are simply not prepared to deal with the complexities of new construction lending which can and do include frequent last minute construction change orders. In addition, an affiliate is committed to the high value a builder places on customer satisfaction because the builder relies on its customers for repeat and referral business.

According to a recent study by J.D. Power and Associates, also cited in HUD's regulatory impact analysis, the majority of borrowers surveyed who financed through a builder affiliate were more satisfied with the financing experience and chose the builder affiliate because its interest rates were competitive and the entire buying process was easier. Moreover, customer service from an affiliate means more accurate moving costs, estimates, and the certainty that the borrowers understand their loan programs. Customer service is a long term view for an affiliate because they focus, along with the builder, on creating communities and enhancing the builder's brand. We don't just do one-off transactions. Contrary to HUD's view, timely closings and extraordinary customer service are the primary business value affiliates provide to homebuilders, benefits to the consumer that far outweigh the income the builders receive from the affiliate ownership.

Affiliate relationships have facilitated home purchases for upwards of millions of consumers over the last several decades. In the market conditions of the past year, as mortgage financing has become unstable and uncertain, affiliate relationships have assumed an even greater importance. Many homebuilders can document hundreds of sales originally scheduled for outside lender financing that have fallen through and were subsequently saved by the builder-affiliated mortgage and title company. Now more than ever, reliable service, accurate forecasting, and competitive pricing offered by affiliates are needed by homebuilders and their buyers.

In truth, affiliates allow builders to manage the business of building and selling homes with greater efficiency, the benefits of which translate into value for the buyer. HUD's proposal fails to account for the savings builders realize through affiliated businesses, which are then passed on to the consumers in its incentives. Contrary to HUD's assertion, homebuilders do not increase the selling prices of homes to offset these incentives. The competitiveness of the marketplace does not allow it.

Beyond the negative impact to builders and homebuyers, we do not believe HUD has established a sound rationale for changing the definition of required use. HUD supports its proposal entirely based on anecdotal, incomplete, and unsubstantiated examples which have been advanced by previously outspoken competitors of affiliated businesses. The problems cited by HUD appear to be violations under the current RESPA regulations and should be addressed as such, but they do not make a case for change.

Furthermore, HUD has provided no empirical studies or statistics substantiating its position that consumers are harmed by the use of builder affiliate service providers. We suggest that in developing this proposal, HUD's research does not conform to the data quality requirements imposed in all Federal rulemaking.

In closing, I will reemphasize that prohibiting affiliated incentives would ultimately increase home purchase costs, undermining critical financing support to the consumer at this time of unprecedented turmoil in our industry. As further detailed in my written statement, NAHB has offered an alternative definition of required use which, if adopted, would continue to permit homebuilders to offer bona fide and reasonable incentives in exchange for buyer's use of affiliated companies.

Mr. Chairman, thank you for this opportunity to share our views and those of the National Association of Homebuilders. I would welcome any questions.

[The prepared statement of Ms. Still can be found on page 285 of the appendix.]

Chairman WATT. Thank you so much for your testimony.

Mr. David Stevens, president, affiliated business, Long and Foster Companies on behalf of Real Estate Service Providers Council, RESPRO, is recognized for 5 minutes.

STATEMENT OF DAVID STEVENS, PRESIDENT, AFFILIATED BUSINESSES, LONG AND FOSTER COMPANIES, ON BEHALF OF REAL ESTATE SERVICES PROVIDERS COUNCIL (RESPRO)

Mr. STEVENS. Thank you. Good morning, Chairman Watt, Ranking Member Miller, and members of the subcommittee. Thank you for the opportunity to speak here today.

Long and Foster Companies is the third largest residential real estate brokerage firm in the Nation with over 200 residential real estate brokerage offices in the 8-State mid-Atlantic region. We offer a full array of mortgage, title, and insurance services through a combination of either wholly-owned or partly-owned businesses.

Today I am representing RESPRO, a national nonprofit association of over 200 companies who promote diversified services for homebuyers, often called one-stop shopping. I share the concerns my fellow witnesses have expressed today in their testimony over the potential impact of HUD's RESPRO rule on these individual industries. I am here today, however, to address the particular impact that the required use provision of the proposed rule will have on diversified real estate brokerage firms and our customers.

The majority of the Nation's 500 largest real estate brokerage firms offer mortgage, title, or closing services. According to a 2008 survey of homebuyers by Harris Interactive, 45 percent of homebuyers chose a one-stop shopping service in 2008 compared to 2002. In today's challenging housing market, which has seen the failure of numerous mortgage and title firms that can threaten prompt and efficient closings, diversified real estate brokerage firms are increasingly using our affiliated companies to enable our real estate customers to close on time. Because we own companies needed to close the home purchase transaction, we are better able to resolve any service issues that arise more efficiently than we could with independent companies.

RESPA prohibits requiring the use of an affiliated provider. HUD has long allowed voluntary incentives to consumers who purchase affiliated services as long as the services are separately available and as long as the incentive is not offset by increased prices of other services in the transaction. Because diversified real estate brokerage firms can ensure more prompt and efficient closing through our affiliated companies, we commonly offer voluntary positive incentives to consumers who use our affiliated services under this longstanding RESPA exemption.

For example, we offered our real estate customers who purchased a mortgage through our affiliated mortgage company, Prosperity Mortgage, a half percentage reduction in their mortgage over the first year, which using a rate of 6 percent saved them $762 on a

$200,000 mortgage. The program was voluntary, and if it wasn't used, the homebuyer paid no more. But if it was used, the customers would have received substantial savings, and we would be better able to ensure that they get to closing on time.

I have described many other examples of consumer incentives used in our industry in my written statement. These voluntary consumer incentives have been well-received by consumers. In fact, Harris Interactive found in its 2008 survey that I referred to earlier that 77 percent of homebuyers consider the biggest advantage of using one-stop shopping programs is saving money through discounted prices. Unfortunately, HUD has proposed in its RESPA rule to prohibit companies from offering these consumer incentives that lower cost and enable prompt and efficient closings. HUD has provided no indication that it has analyzed the types of consumer incentive programs being offered throughout the industry today that provide consumers tangible savings and better service.

Mr. Chairman and members of the subcommittee, HUD's proposed ban on voluntary consumer incentives is another example of how HUD's proposed RESPA rule would increase costs and result in poorer service for homebuyers. The rule was not well-conceived as a whole. Given the breadth of HUD's proposed RESPA rule, and its potential impact on today's fragile housing market, we believe that HUD should withdraw its RESPA regulation and work with the Federal Reserve Board to develop uniform mortgage disclosures that would truly accomplish its goals in rulemaking.

Thank you for the opportunity to testify, and I would be glad to answer any questions.

[The prepared statement of Mr. Stevens can be found on page 277 of the appendix.]

Chairman WATT. Thank you for your testimony. I thank all of the witnesses for their testimony and for being very timely. Almost everybody came in right at the 5-minute limit, or under the 5-minute limit in some cases, and we appreciate that.

We welcome Mr. Royce, who is a member of the subcommittee, Mr. Perlmutter, who is a member of the subcommittee, and Mr. Hinojosa, who is not a member of the subcommittee—

Mrs. BIGGERT. Mr. Chairman, may I just correct something that I said about the letter?

Chairman WATT. The gentlelady is recognized.

Mrs. BIGGERT. Thank you. The letter that I referred to that was being sent to OMB from me, Representative Hinojosa, and others has not been sent yet. It will be very soon. I had said that it had been sent yesterday, and I did not want people to think that they did not receive it.

Chairman WATT. We will make that clarification and modify the unanimous consent request to insert into the record the final letter when it is sent, because the record will still be open at that point.

I welcome Mr. Hinojosa, who is not on the subcommittee, and I would ask unanimous consent at this point that Mrs. Biggert and Mr. Hinojosa, who are not members of the subcommittee, be allowed to engage in the questioning of witnesses at the end of the subcommittee members' questions. Without objection, it is so ordered. Both of them have a very, very strong interest in this issue. In fact, they both led the letter that was sent to HUD originally

and obviously are leading a subsequent letter that is going to OMB now, so they have strong feelings about this and strong knowledge about it also.

We thank the witnesses for being here and for covering a wide range of issues related to the proposed rule. There are some differences of opinion within the panel. I thought it would be just a consistent flogging of HUD, but we may have some interesting interchanges within the panel also.

I am going to now recognize members of the subcommittee, and subsequently members who are not on the subcommittee but are members of the full committee, to ask questions, each for 5 minutes. And I will defer my questions to the very end to allow other members to go in case they need to leave. I will start with Mr. Lynch. He is recognized for 5 minutes.

Mr. LYNCH. Thank you, Mr. Chairman, and Ranking Member Miller. I appreciate the testimony that has been offered this morning. Let me just say at the outset that I share much of your concern regarding the HUD proposed rule.

However, with that being said, I do want to caution—a number of you this morning have talked about the cost of regulation, and I just want to remind you of the cost of no regulation. As we know, much of this subprime mortgage crisis came out of a process that was completely unregulated with respect to mortgage brokers. The no-document loans, the no-document mortgages, the liar loans, the liar mortgages, all of that went out the door without substantial regulation as compared to banks, and I think there was an outsized representation of those bad mortgages originated by mortgage brokers as opposed to banks that were more heavily regulated and overseen.

I am not saying there was no regulation, I am just saying there was less regulation of our mortgage brokers. So when I hear that we don't need additional regulation of the mortgage brokerage industry, it is sort of like the captain of the Titanic saying we don't need more lifeboats, and making the statement from the deck of the Titanic, because we are obviously having a very difficult time.

I thought, Mr. Kermott, your observation that you—you are trying to correct these weaknesses at the closing, it is a bit too late. I have been the victim of enough closings, I should say, to know that there is only so much you can accomplish on that day, at that moment. You have eight people at the table, and seven of them are being paid only if the closing goes through, so it is a very difficult situation to try to catch the runaway horse at that point. I agree with that very succinct observation.

However, given the fix that we are in—and I understand that the HUD proposal has many weaknesses in it, and I understand that there is a disparity between where HUD is going and where the Fed has gone with respect to the Truth in Lending Act, and it is almost apples and oranges when you look at the two proposals and the two approaches by both of those agencies.

I am going to ask Mr. Savitt and Mr. Kittle to have a first whack at this since I have mentioned them in my opening remarks. Do you think we should try to reconcile the approaches by HUD and by the Fed with respect to the Truth in Lending language, or do you think that we should start from scratch on both and try to,

rather than harmonize the two existing proposals, just go back to square one and try this all over again?

Mr. SAVITT. Mr. Lynch, first I want to, if you don't mind, I would like to address one of the comments that you made about—

Mr. LYNCH. I expect that.

Mr. SAVITT. Okay, about the subprime. First of all, mortgage brokers are regulated in every State in this country and the District of Columbia. As a matter of fact, in some cases we are more regulated than other originators, loan officers who work in banks, for example. But most importantly, dealing with the subprime issue, mortgage brokers did not develop the loan products. They did not develop subprime products.

Mr. LYNCH. Fair enough.

Mr. SAVITT. We didn't set the guidelines, we don't underwrite, and we don't originate those loans. We sold the loans that were created by others. So I think to characterize mortgage brokers as the ones that caused the problem with subprime loans, I think, is a little—

Mr. LYNCH. I think I conceded in my opening statement, I said I realize that a lot of the weaknesses and frailties are in the underwriting process. However—and again, there is involvement by the broker, there is involvement by the rating agency that gave it a triple A rating, there were failings all along the line. I am just trying to give you your share.

Mr. SAVITT. I appreciate it. Plus there was a—

[Laughter]

Mr. SAVITT. We have taken more than our share, trust me.

Mr. LYNCH. Probably.

Mr. SAVITT. There was a GAO study that was commissioned by Chairman Frank and Ranking Member Spencer Bachus, and the purpose of that study was to show what happened with the mortgage meltdown, with the housing crisis in this country, and particularly if mortgage brokers were the culprits, and mortgage brokers were vindicated within that study. One other study by Georgetown University showed that by using a mortgage broker for a subprime loan, a consumer would save on average 1.13 percent on their annual percentage rate. So I thought it was important to bring that up.

But as far as your question about HUD and the Fed, I think it is important that they do harmonize. I think that would solve a lot of the problems.

Mr. LYNCH. Okay. Thank you, sir. Mr. Kittle?

Mr. KITTLE. Mr. Lynch, thanks for the question. May I also open with just a quick comment?

Mr. LYNCH. Oh, absolutely.

Mr. KITTLE. Okay. I am sure you expect it.

Mr. LYNCH. Yes, sir.

Mr. KITTLE. It is not, and we will defend this statement and can, it is not necessarily the products that caused the problem. They were just made to the wrong people, because 85 percent of those products are still paying on time at the end of the day. So I just want to make that point clear, that the cause for foreclosure—and we are not here talking about that, but we are talking about the

issues—the three top causes are unemployment, divorce, and healthcare. They weren't the products themselves.

But to answer your question, we do think that it is time for the Fed and HUD to sit down together. HUD mentions through its own—it states through its own actions, the documents that I held up during my 5-minute testimony, that it is so confusing that they have to make a map to explain to the consumer. So this is onerous, it is over the top.

I am going on my 31st year in this business, and when I got in the business back in the 1970's, I had to disclose Truth in Lending and calculate it at the application by hand. I didn't have computers, we didn't have PDFs and cell phones, we had to calculate it out.

Part of the issue is the education process. We put information in the computer and it spits our forms out. The people taking the loan applications need to be educated on the forms they are giving to the consumer, so we advocate not only for pulling this RESPA law, but advocate also for education of the people who are taking the loan applications.

Mr. LYNCH. Mr. Chairman, I yield back.

Chairman WATT. I thank the gentleman. Ranking Member Miller is recognized for 5 minutes.

Mr. MILLER. Thank you. I took the cost of regulation a little differently than my good friend Mr. Lynch did. I took you meaning the cost of inconsistent regulation, was what I took in your statements. And I agree, the cost of inconsistent regulation can have a very negative impact on the marketplace.

Mr. Lindsey, you had said the small lenders would be pushed out of the marketplace based on this regulation. Can you further elaborate on that, please?

Mr. LINDSEY. Thank you, Ranking Member Miller. The concern that we have is that the way that the regulation is proposed right now, it would offer an opportunity for the larger lenders to put forth a package of guaranteed services and that would in fact allow them to use their market clout to press down the prices, which ultimately would lead to smaller lenders or smaller service providers being anti-competitive, and perhaps even having to cut back on the services that they provide in order to meet those prices that would be required for them to be included in these packages. So if they are not included in the package, they have lesser opportunity to present themselves to the marketplace, and invariably, they would probably be pushed out of the market.

Mr. MILLER. Thank you. Ms. Still, you said there would be an immediate negative impact on the marketplace. Could you further elaborate on that?

Ms. STILL. Well, certainly a negative impact on the efficient operations of the homebuilders, and definitely a negative impact on the consumer. If you look at the value of the incentive, that which is offered by the builder and is a reflection of the builder's benefits, we take the economic value, certainly, away from the consumer. We would also take away from the consumer the ability, if you will, to understand the value that a builder affiliate brings in its years of expertise in a new construction environment. New construction lending is different than lending in an existing environment. We

would not be able to appropriately demonstrate to the consumer the efficiencies that we could create through the coordination of affiliates, the commitment to customer satisfaction, and the long-term view.

We do not believe as mortgage affiliates we do transactions. We build communities, we want our communities to perform, we want our communities to perform 1 year, 2 years, or 3 years down the road. We sell lifestyle. So we take great care in making sure that our buyers understand the loan programs that they are choosing, make sure they understand their total move in cost estimates, and make sure there are no surprises at the closing table.

Mr. MILLER. It seems to be a common complaint that you hear among people who are buying, that they were given an estimate, and when the closing process occurs, all of a sudden things start to pop up. I know HUD has tried to deal with that through their proposal.

Somebody very close to me, it happened to them where they got the good faith estimate and they had a lock-in date on their rates, so they had 3 days to close or they were going to lose their rate, and all of a sudden some points and fees start to appear that they weren't expecting, which they really can't do. HUD tried to fix it.

If you don't agree with the rule, how would you think that could be better handled? Yes, Mr. Kittle.

Mr. KITTLE. Well we have proposed to HUD a very simple GFE and a new HUD–1. They have had it for almost a year.

Mr. MILLER. It is the same as basically the upfront good faith estimate?

Mr. KITTLE. Right, but the difference is that all the lines match. I mean, that isn't real rocket science. You can't have predatory lending until you lend, which is what you are saying. So when a consumer goes to closing, whether it is a first-time homebuyer or somebody who has bought 20 houses, elderly, minority, if all the lines match, then you can't change fees and points, and if you do at that point, the customer always has the right to back away from the table.

Mr. MILLER. And to clarify, you are not arguing against regulation, you want consistent regulation is the biggest concern I heard from all of you when we—

Mr. KITTLE. Well let me go to Debra Still's point in her testimony, which was a great point and we all need to take it away today, is that there is a lot of regulation on the books right now, a lot of laws, and they are not being enforced by HUD. Maybe we should enforce what is there. Regulation is great as long as it is not onerous and it doesn't add cost to the consumer.

Mr. MILLER. And everybody understands what it is.

Mr. KITTLE. Everybody understands it; it is clear and transparent.

Mr. MILLER. Now the Federal Reserve Board's comments on the proposed RESPA rule discuss how HUD and the Fed should harmonize TILA and RESPA, the disclosure. They discuss how the different disclosures are duplicative and inconsistent. Would you agree with these comments and how would you ensure consumers receive disclosure in a competent printed manner, and how would consumers react to multiple disclosures? Whomever would like to

answer that one. It is a three-part question, so take any part. Yes, Mr. Savitt.

Mr. SAVITT. Mr. Miller, as we know, in addition to the Fed, the Federal Trade Commission has also weighed in on this with two studies from 2004 and 2007. The 2007 study was even more extensive than 2004, and it talked about these different types of disclosures, that they were too complicated, there were too many of them, and that we needed to simplify this process for the consumer, and they even came up with some other type of—in addition to the Fed having some ideas of how to disclose, the Federal Trade Commission also came at it with their own form.

So I think what we really need to have here is the Federal Trade Commission, the Fed, and HUD sit down, and I know it would be unprecedented, but if the three of them would sit down and harmonize their forms together—and I know we are adding one more into the mix here with the FTC—but I think if we did that and we listened to the one agency that is charged with protecting the consumer, that being the FTC, I think we would have the right forms for the consumer—there probably would be less forms—but the right forms for the consumer that would make it easier for them to understand the transaction, thereby avoiding problems when they got to closing.

Mr. MILLER. I agree with that.

HUD is proposing to address this in a booklet form. Do you think people are really going to take the time to review the booklet to try to comprehend inconsistent loan terms? Yes, Ms. Still.

Ms. STILL. Yes, I might mention, using an example from my company, we conduct a disclosure conference call one week after loan application, and it is to provide the customer in assisted fashion to go through all of the disclosures that they have to sign even today. And as an independent mortgage bank with State disclosures as well as Federal disclosures, today it is a 45-minute phone call. On average it takes 45 minutes to make sure that the borrower truly understands the initial Truth in Lending Disclosure, the good faith estimate, and all of the State disclosures. We have to have a comprehensive approach for Federal disclosures, or that call is just going to get longer.

Mr. MILLER. Mr. Stevens?

Mr. STEVENS. It is interesting, and you referred to Mr. Miller in having recently had a friend who closed a mortgage and the surprises at the settlement table or prior to that with things changing.

Between the deed of trust and the promissory note, all the disclosures, I really question today how deep a consumer goes into each one of those documents. We provide every consumer a glossary of terms, which is actually prepared by HUD, that we present to our consumers so they understand what kind of mortgage product they are getting. The challenge that we see, if you go through the actual good faith estimate document, I can't see anything that will confuse a consumer more than this new document that would be added to the additional documents they get already.

So while we all agree that we need to come up with better ways to disclose mortgage products, particularly option ARMs and the kind of things that caused so much trouble over the last 24 months particularly, this will just do nothing more but confuse. As a mat-

ter of fact, I don't even think it explains the ARM very well in the questions it asks, and I think consumers will walk away just with more confusion.

Mr. MILLER. Well I want to thank you all for your comments. They have been very productive, and I appreciate it very much.

Chairman WATT. I thank the gentleman for his questions. Mr. Perlmutter is recognized for 5 minutes.

Mr. PERLMUTTER. Thank you, Mr. Chairman, and thank you, Mr. Miller, for convening this panel. And I just want to thank the panel members here because all of you know your stuff. We have sort of been on the downside of the market and everybody is in kind of emergency mode here, but I just appreciate this.

I want to tell you the framework I am coming from. First, with respect to RESPA, we are dealing with the biggest transaction in most people's lives, and that is the purchase of a home, so we start there. Now how we got to this panel today, I would say, there was a lot of money chasing a lot of transactions, a lot of loans. And so as time went on, the products got riskier because the borrowers became less creditworthy, in my opinion, just having been sitting up here for a long time and listening to these kinds of things.

Mr. Stevens, and here is really the dilemma I have and that all of you have, and that is convenience versus sort of confidence or, potentially, confusion. But convenience in the transaction versus confidence in the price of a different—other than just the purchase price, but the price of all the ancillary services. Or I think it maybe was you, Ms. Borne, who said this, but it is comprehensive versus comprehensible. The more comprehensive it is given the myriad of products that we have now, the more incomprehensible this form is going to be, or the least useful the form is going to be.

There are a lot of things up in the air, so let's get back to basics. What is the purpose of the good faith estimate? Let's start with you, Mr. Kittle, you have been through the wars on this thing. What is the purpose?

Mr. KITTLE. Well, the purpose is, at the loan application, to disclose to the customer in good faith that these are the costs that they are going to incur for the purchase of their home. And it is called the good faith estimate because those costs can change under certain circumstances. If the house doesn't appraise that they are buying, they may have to go back and re-negotiate the price, therefore it changes. If they, during the process, decide that they may want to change loan programs, a whole new disclosure has to be made and then re-disclosed with a new good faith estimate. So there are situations when things change. That is why it is an estimate of cost.

Plus, there are two things on there that we don't know for sure at the loan application. That is when the loan is going to close, so we have to estimate the amount of daily interest they pay to closing date to the first of the next month, and the estimated property taxes. The title search hasn't been done yet, we have to make sure that those things are accurate. So many of the costs on GFE are exactly what we know. There are some that can change.

So when we go to closing we need a HUD–1 settlement statement that matches up line for line. Each one of these lines are numbered. Why can't they, why shouldn't they match up? And that

is a rhetorical question. So when the customer goes to closing, they can say "Oh, you said it was going to be $300 for an appraisal, why is it $375?" Or, "You said my interest rate was 'X,' why has it changed?"

Mr. PERLMUTTER. No, I am with you 100 percent, and these forms—

Mr. KITTLE. But that is why we have a good faith estimate.

Mr. PERLMUTTER. Some of these forms make it very complicated for the borrower, but on the other hand, you have this myriad of products. Now maybe I am living in antiquity, but I thought RESPA, I thought these forms were the result of a fear of tying arrangements, of anti-competitive combinations between the real estate brokerage firm and the mortgage company and the homebuilder all—

Mr. KITTLE. We had a good faith estimate before we had RESPA laws.

Mr. PERLMUTTER. But I thought RESPA, which is what—okay, so you answered as to good faith estimate. Let's talk about RESPA. Now, with respect to RESPA, which is the intention to try to modify RESPA a little bit or these good faith forms, how do we take into effect then this—or should we just get rid of sort of this fear of tying arrangements?

Mr. KITTLE. Now, we just want—and I will finish this and turn it over to Mr. Savitt—what we are advocating is, one, the Federal Reserve and HUD to sit down together and work this thing out. Not only do we need a GFE that is clear that matches the HUD–1, let's get it all done at the same time and get TILA reform also. The most confusing form at loan closing and application is the Truth in Lending, the four blocks across the top, the APR disclosure. That is the most confusing form. The one where predatory lending can happen is not the TILA, though, it is when you get to closing and costs have changed on the HUD–1 from the good faith estimate. You match lines with numbers, it makes it harder for it to have predatory lending and change the fees and costs.

Mr. PERLMUTTER. And then Mr. Savitt, and then I would like Mr. Lindsey to talk about—I guess my concern is, do we need to worry about tying arrangements and any of that in these forms? From my experience, that was one of the key pieces of it all.

Mr. SAVITT. Well, the first thing I would like to say is that I agree with Mr. Kittle about the one page disclosure of the good faith estimate. There is a sound bite for you. And the problem that we have with—well, let me just address this.

Some of my colleagues here today spoke about the required use section of RESPA. This is something that I know quite a bit about. I have been researching this for the past 4 years based upon complaints that I first received from my customers and then also working directly with HUD. The number one complaint that HUD has, according to HUD, are complaints over affiliated business arrangements.

Now affiliated business arrangements are not bad. We are not advocating outlawing them. They are required, these companies are allowed—builders, for example, and mortgage companies are allowed to offer a discount to the consumers provided it is a true dis-

count and it is not made up anywhere else in the transaction, and we are fine with that.

The problem comes in under the tying arrangement, where you mentioned, Mr. Perlmutter, where you have a builder who offers, perhaps, a $5,000 assistance towards closing costs, maybe an upgraded kitchen, a swimming pool, we have seen cars, we have seen all kinds of things, but it is contingent upon the required use of a specific settlement provider, namely a mortgage company and a title company. And what we have found is that in many cases, the interest rates charged in the beginning, or the interest rates disclosed on the good faith estimate in the beginning, are not what happens, are not what materialize when you get to closing because you are not locking in the interest rate when you first file your application with the builder, in many cases because houses usually take 4 to 6 months to complete.

So what happens is when you get down towards the end, maybe 30 days out when they give you the interest rate, at that point the interest rate is substantially higher in a majority of the cases. So if you try and get out of the transaction to use an outside lender, the first thing they tell you is, "You are not getting your $5,000 towards closing costs. We gave you an upgraded kitchen at a cost of $20,000. You need to write me a check for $20,000 and if you don't do that, you are in violation of your contract, and we are going to void your contract and keep your deposit."

So there is a major problem with tying arrangements.

Mr. PERLMUTTER. My time has expired, and maybe the chairman will allow another pass through the panel, but I appreciate—

Chairman WATT. I think Mr. Stevens at least wants to respond, so we will give him equal time to respond.

Mr. STEVENS. Thank you, Chairman Watt. There are just two minor points I would like to make sure we have on the table.

One is that the current RESPA law requires that these tying arrangements, that affiliated business arrangements must be disclosed to the consumer, which we do upfront in our industry, and there is a separate disclosure. For example, if you use a Long and Foster agent to buy a home and you use affiliated businesses, that disclosure is all clearly provided to the consumer at time of real estate contract submission, not at the end. So that is already covered in the RESPA provision. That is one key point.

The other thing I would just like to add is in the written statement that I provided all of you, I gave examples in that statement of some discounts we have used. Those are true subsidies. We lost revenue on those provisions that we provided to consumers. They are typically short-lived, but they were consumer benefits, and it was only through the value proposition of being able to have a full service real estate company that has all of these services together that we could, in essence, do that. But it was a direct benefit to the consumer, it was less revenue than we would have realized on the transaction, and less, we believe, than competitors could provide on that transaction unless they offered the same kind of discount. It is a direct consumer benefit, and that is the key point I also would like to add.

Thank you.

Mr. SAVITT. Mr. Perlmutter, may I clarify my statement? What I was speaking of is tying of incentives to the required use of a specific service provider. I am not talking about the disclosure, the affiliated business arrangement disclosure. Thank you.

Chairman WATT. I thank the gentleman for his questions. Mr. Hinojosa is recognized for 5 minutes for questions.

Mr. HINOJOSA. Thank you, Mr. Chairman. First of all, I wish to thank Congresswoman Judy Biggert for joining me to lead the effort to try to bring us to the point that we are having this congressional hearing which Chairman Watt has helped us bring before Congress.

I found the testimony given by each one of you to be very informative, and I believe that we make the case for what we were trying to do in the letters that were sent August the 7th, August the 18th, and May the 5th between HUD, and now the next letter that will be going to OMB. But I want to ask that you raise your hand if any of you know the content of the revised RESPA proposal as submitted to OMB.

[No hands raised]

Mr. HINOJOSA. Not one of you.

Mr. Chairman, I think that we need to know that this process has not been what it should have been in order to have something that is good for those borrowing monies for home mortgages, nor the lenders.

I have another question: Do you agree that OMB should reject the revised RESPA proposal and send it back to HUD with instructions to reopen it for a 60-day comment period and work with the Federal Reserve as it revisited the Truth in Lending Act? Raise your hand if you are in favor of that.

[Every witness raised their hands]

Mr. HINOJOSA. Thank you. I want to express my appreciation to you for holding this important and timely hearing on a flawed, misguided, and seemingly mysterious proposal by the Department of Housing and Urban Development to amend the Real Estate Settlement Procedures Act, commonly known as RESPA. I ask for unanimous consent that my entire statement be included in the hearing today. Thank you. I also want to take some excerpts from my statement because I want to make some points.

I believe that it is the responsibility of Members of Congress who sit on this increasingly important committee to ensure that HUD does not alter RESPA to the detriment of consumers, the home buying process, and ultimately the economy of the United States which relied so heavily in the recent past on the strength of the housing market to sustain itself.

I believe it was on May 5th that Congresswoman Judy Biggert and I sent a letter to HUD's Deputy Secretary Roy A. Bernardi requesting that HUD extend the comment period on the proposed RESPA rule change by 60 days, and all they gave us was a 30-day extension. On August the 7th, Congresswoman Biggert and I sent a letter to HUD addressed to Steven Preston, the Secretary of HUD. The letter requested that HUD withdraw its flawed proposed RESPA rule and immediately commence a joint rulemaking process with the Federal Reserve Board to produce more simplified mortgage and real estate settlement cost disclosure forms.

On August the 18th, HUD hand-delivered a document that they claim to this day is the response from the Secretary of HUD to me and to Congresswoman Biggert and the other 242 Members of Congress who signed the letter. It is important for the record to show that the Secretary of HUD apparently did not have the time nor the inclination to respond to a letter signed by 244 Members of Congress. Instead, he had his Assistant Secretary for Governmental Affairs author and sign the document which was the response we got. I thought that was insulting, not only to Judy and to me, but I believe to the other 242 Members of Congress who co-signed the letter.

Now let's look at what we think is the next step. No one other than HUD and OMB knows the content of HUD's revised RESPA proposal. I think its revised proposal needs to be vetted by consumers, by industry, and by Members of Congress. Now that the revised RESPA proposal has been submitted, OMB may take one of three actions: One, reject the revised proposed rule; two, send it back to HUD to be published in the Federal Register as final; or three, return the revised proposal to HUD with instructions.

Cpngresswoman Biggert informed you earlier today that we co-authored and co-signed a letter to OMB requesting that they reject the revised RESPA proposal and send it back to HUD with instructions to coordinate with the Board of Governors of the Federal Reserve as well as other relevant Federal agencies. The letter will be sent out today. Chairman Watt, HUD received almost 12,000 letters opposing its proposed rule—244 Members of Congress signed a letter to HUD requesting that it withdraw its proposal and commence a joint rulemaking with the Federal Reserve Board as it revisits the Truth in Lending Act. Everyone on this panel wants OMB to send HUD's flawed RESPA proposal back to HUD with instructions. I cannot stress how important it is for OMB to send the revised RESPA proposal to HUD with instructions.

I ask unanimous consent that copies of these three letters that I have been making reference to dated August the 7th to Honorable Steven Preston, Secretary of HUD, August 18th letter to Judy Biggert and to me, which was the answer that I referred to by the Assistant to the Under Secretary for Congressional Affairs, and the third one is dated May the 5th, which we sent to the Honorable Roy A. Bernardi, Deputy Secretary, and I ask unanimous consent that they be included in today's record.

Chairman WATT. Without objection, it may be that all parts of those have already been submitted for the record prior to your coming in, but we will make sure that they enter the record in their entirety.

Mr. KITTLE. Mr. Chairman, if I could, I just want to commend the Congressman, say well done, and Congresswoman Biggert, thank you for getting that done. Well done.

Mr. HINOJOSA. I have one last question before I conclude. I think that the mess that we are in, the subprime mortgage loans contributed to the crisis we face in home construction today. But let's look at the possibility—and I want somebody to answer this. What would be the impact of the proposal that the adjustable rate mortgage for home loans be prohibited for a period of not less than 5

years? Could somebody answer that? What would be the impact? Yes?

Mr. KITTLE. If I understand the question, you would prohibit all adjustable rate mortgages for up to 5 years?

Mr. HINOJOSA. It has been a mess.

Mr. KITTLE. But was that the question?

Mr. HINOJOSA. It was explained in one of our hearings that there were people who could possibly use it to buy a house and flip it in a short period of time, but it made a mess out of the situation that we have today. And my question to you is, there are lots of options available for me or anyone else to borrow money and be able to buy a home. If you were to take ARM from one of those options, what would be the consequences? Because I certainly am prepared to take congressional action and ban that from the list at least for 5 years so that we can see if we can straighten out the mess that we have.

Mr. KITTLE. I think that would be an action that we would be totally against. I think it would be inappropriate for this reason: Adjustable rate mortgages, when given to the right customer with the right caps and margin disclosures are an effective tool. Back in the early 2000's, 2001, 2003, they were actually as much as 35 percent of the loan production that was out there. They represented 35 percent of the business. They weren't subprime ARMs, they were good, solid 3/1, 5/1 adjustable rate mortgages that were sold to the GSEs and private investors.

They are an effective tool. They are not the ones that are delinquent. You can flip a house regardless of a program that you take. You can flip a house on a 30-year mortgage. So it doesn't make any difference whether it is an ARM, a pay option ARM, an FHA loan, or one that goes to Fannie or Freddie. So I think that is confusing the difference between flipping and an adjustable rate mortgage, so we think that it would hurt business and it would hurt—FHA has a great program right now.

Mr. HINOJOSA. Let me ask Rebecca—

Mr. KITTLE. A 1-year ARM that would—

Mr. HINOJOSA. Fine. I understand everything you said. I want to ask Rebecca Borne, as representing the Center for Responsible Lending.

Ms. BORNE. For many years, adjustable rate mortgages have been made and underwritten responsibly, and they didn't create the crisis that we have seen today. Far more responsible for the crisis has been the 2/28 and 3/27 teaser rate loans where consumers were sold super low rates for 2 to 3 years and payment option ARMs, whose teaser rate may last as long as 1 day. Those were toxic products and they were not properly underwritten. The borrower's ability to repay was not properly assessed in many cases. So I think that we would be more likely to recommend an approach that addressed proper underwriting standards and addressed some of the broader perverse incentives in the market, from the secondary market all the way down to the broker, such as assignee liability, before we would recommend banning all ARMs for a 5-year period.

Mr. HINOJOSA. Thank you, Chairman Watt.

Chairman WATT. I thank the gentleman and to the extent that members of the panel have additional responses to this question, you are welcome to submit them in writing. It is really not the focus of this particular hearing, but I didn't want to cut off discussion of that issue. It is a novel idea and I suspect everybody on the panel would be uniformly opposed to it in this breadth, at least even though those who have some concerns about the way adjustable rate mortgages have had impacts in the marketplace.

Mr. Manzullo is recognized for 5 minutes.

Mr. MANZULLO. Thank you, Mr. Chairman. When I practiced law and was involved in at least a couple thousand closings, it was apparent to me that the more people who are involved in closings, the more the consumer is protected. We found that through the analysis of taking and looking at the closing statements, we would get figures in to the title companies that the attorneys involved, the Realtors, the bank, and there was always that backup that you had an independent set of third eyes that would take a look at the closing statement.

I have a question to Mr. Kermott and Mr. Lindsey. In your testimony you discussed your organizations' opposition to so-called volume discounting. These are the big guys. I believe volume discounting is a veiled attempt to reintroduce the concept of bundling services. In the hearings that we had when I chaired the Small Business Committee in 2003, the long-term impact of volume discounts is to eliminate competition and destroy small businesses. However, HUD has indicated that people have never been to a real estate closing expect perhaps their own, and then they brought in a lawyer. HUD has indicated they feel that volume discounts are not a repeat of bundling.

I would like to ask you if you agree with that assessment. Can you discuss the impact that volume discounting would have on title companies and other small businesses and also on the Realtor profession?

Mr. KERMOTT. Yes, thank you for that question. We agree with your assessment. The members of the American Land Title Association, we have both large companies and small companies, but we are uniformly against HUD mandating or encouraging volume discounts. On the one hand, it is hard to argue against lower prices for consumers. But to mandate it or to pave the way for larger companies to have a competitive advantage is not the way to do that.

In fact, volume discounts would be discriminatory. It would discriminate against smaller companies who don't have the relationships with large volume lenders, so they can't offer a volume discount, and it would also discriminate against consumers who are not dealing with a lender who has that network of service providers. For instance—

Mr. MANZULLO. Mr. Lindsey, why don't you pick it up—I don't want to run out of time—and then we can come back.

Mr. LINDSEY. I concur with what Mr. Kermott said thus far, and I think what we would like to add to this, though, is that there is also the component of value.

At the local level, for example, real estate professionals have relationships with smaller vendors and smaller providers who provide value and are more accustomed to the local practices and cus-

toms in that particular marketplace that have real applicability to the transactions. And if we are allowed to suppress the pricing so that those local providers are unable to compete and therefore are then pushed away, then we eliminate the choice option that we have. We also will expose ourselves to the potential of a reduced set of value that is actually being delivered. And ultimately, when it is all said and done and all the dust clears, there is a strong likelihood that prices are going to go up again because we have reduced competition.

Mr. MANZULLO. What has always bothered me about HUD, and the fact that the people who draw this up have no real estate experience, is that they come out with the outrageous statement that a consumer will save $1,000 at closing if bundling is allowed. They have never been able to answer the question of what cloud they picked that from.

Plus, my understanding as I take a look at this four-page monster and the other one called TILA, I guess "TILA the HUD," if that is what you want to call it, is the fact that real estate closings, when I closed them, would take a half hour. When my wife and I bought a townhouse out here in 1996, it took 3 hours, we were told not to bring our kids with us, and I had to hire an attorney to go through those documents even with the vast experience that I had. Now HUD, again, has made it even messier.

But my understanding, as I look at those documents, is if there is a kickback arrangement between a lender and a real estate company, that does not have to be disclosed if the bundling takes place. Isn't that correct?

Mr. LINDSEY. That is our understanding as well, and I think we also have a further concern that when in fact this bundling occurs, we don't have a breakout of the actual services that are involved. So sometimes you might have a person show up at closing, and there is a charge on there which they had no knowledge of in advance of that.

Mr. MANZULLO. You mean the so-called document fee?

Mr. LINDSEY. Yes, or commitment fee, or many other fees that would be allowed to be included.

And just recently looking at the settlement statement and comparing it to the GFE, for example, the title charges are not broken out, and there are a number of title charges that would be discrete and shown on the existing HUD–1 settlement statement that have now been combined, and those include attorney fees in some States that are attorney closing States, like North Carolina, for example, where there is no place on that good faith estimate for an attorney's charge for settlement services.

So this bundling of things is really just obfuscating the process further, and we think actually complicating it more and making it less simple.

Mr. MANZULLO. So they create the problem with the bundling, and then they come up with a disclosure that does not show where any misuse or abuse would take place in that. I had a good friend who bought a piece of real estate from a very large real estate company, and they, of course, had their own mortgage company. He ended up with two closings because of the war that broke out because he did not want to use their lender. I guess he finally told

them, “I can pick my own lender. Don’t force me to go with your lender.”

No one talks about that coercion that takes place with the consumer, and that is why I think the consumer groups ought to be out fighting this bundling, because any time you have a relationship—some people are starting to itch out there, and you should—any time you have a close relationship between a real estate firm and a so-called preferred lender, that does not help out the consumer because so oftentimes the consumer is simply talked into it and does not have the opportunity to shop on it. I am not saying that the rate may not be more competitive, it may be, but it just puts more pressure on the consumer.

Thank you, Mr. Chairman.

Mr. STEVENS. Mr. Chairman, may I make a comment?

Chairman WATT. Mr. Stevens, I think, wanted to respond to your last comment, so we will give him that opportunity.

Mr. STEVENS. Thank you. Again, just two reminders that we always like to make sure that we emphasize when this discussion comes up.

First of all, the required use provision exists in the existing RESPA law, so you cannot require the use of an affiliated business as part of the real estate transaction. That is prohibited today, the law is in effect, it has been so for 16 years, so that does exist. I think you make a great point.

I would like to look at the other side. In August of 2007, one of the largest home lenders in America out of New York failed, and we were presented with hundreds of transactions at Long and Foster that could not settle in the subsequent days and weeks that had been committed to, locked, and approved by this lender, and only by having our own companies, in-house, where we control the process, could back up our commitments, could we make sure those transactions closed. It saved literally hundreds, and I would be glad to submit the actual number for the record during that period, and that was literally from just one institution—

Mr. MANZULLO. Well, that was okay in that crisis, but in Oregon or Illinois, a town of 3,500, and throughout the country, the power of the largeness, as it were, of your organization could actually hurt the other people. That is what they are concerned about.

Mr. STEVENS. Could hurt other people in what way?

Mr. MANZULLO. Because of the bundling that you—you go into an area, and you have a whole panoply of your—you have your appraisers, you have your surveyors, you—the so-called one stop shop, that is really the job of the Realtor, because I have seen Realtors, Realtors go out there and they fight for their client to get the best rates on mortgages, to find the people who have the best reputations in the individual trades. And as these people come together, they don’t have intertangling interests. They are there looking out for the consumer because the consumer hires them directly.

And my concern, and this is just in general terms, is that the more you bundle these services to make it so-called easier for the consumer, the more likelihood there is that mischief could take place to the little people who don’t have the opportunity to be as large as you are. And again, that is not an accusation, that is just a general statement.

Chairman WATT. Ms. Still?

Ms. STILL. I would just only point out that the difference between a true discount and offering an incentive of value is different than bundling services and not accounting for those services.

Chairman WATT. I thank the gentleman for his questions, and I think the time has come for me, finally, to ask some questions, and I will yield myself 5 minutes.

My philosophy at these hearings is to try to get as much into the record of varying opinions as we can, not to pit people against each other, but I think it is helpful to hear all sides of an issue. By and large, everybody has been uniformly opposed to HUD's proposed regulation in some respect, so that is a consistent thread. But there are some potential inconsistencies in the panel that I would like to explore just a little bit.

Ms. Still and Mr. Stevens strongly advocated the—I guess it is an affiliate service issue. I would like to get on the record Ms. Saunders' and Ms. Borne's perspective if your organizations have a perspective on the affiliated service position. We have seen some indications of the conflict with Mr. Manzullo's questioning, but Ms. Saunders, Ms. Borne, do your organizations have positions on this issue?

Ms. SAUNDERS. Yes, but it is short and sweet. If, to the extent that an affiliate is required, we think that the total cost of the loan, not just the services provided by the affiliate, need to be disclosed and reduced, which I think goes to many of the comments that we have heard today.

The critical point is that consumers, when they are buying a house or obtaining a mortgage, very rarely shop for specific settlement services. They shop for the total cost of the loan. It doesn't matter to them which particular provider they use, it matters how much money they have to come up with, how much money the loan is going to be extra because of these closing costs, and what is the cost of the loan.

Chairman WATT. Ms. Borne.

Ms. BORNE. We agree with the National Consumer Law Center on that. We would only add that we do support HUD's clarification of the definition of required use to provide that using a preferred provider should not produce an incentive or disincentive for consumers.

Chairman WATT. Okay. I wasn't trying to create a point, counterpoint, I just wanted to make sure that we have in the record everybody's perspective on it if there are varying perspectives on the panel.

The second issue is—do you have something that you wanted to add to this point, Mr. Lindsey? Go ahead.

Mr. LINDSEY. Yes, if I may, Mr. Chairman. The one point that we have sort of glossed over is that the enforcement of this is really one of the critical components of this. We don't find there is a really big problem with having affiliated relationships provided we have enforcement that weeds out the bad actors. There was a very good example that Mr. Stevens gave that there really is a substantial difference between cost and price here, and if a vendor is able to reduce cost and therefore pass that along through an arrangement where there is an affiliation, we don't find that to be a dis-

advantage to the consumer necessarily. But what we do need to do is to weed out the bad actors. So enforcement needs to be really beefed up, I think.

Ms. STILL. And if I could just go on the record—

Chairman WATT. Ms. Still, I think, is about to agree with you.

Ms. STILL. Yes, if I could just go on record and absolutely agree with Mr. Lindsey that there is current regulation. Current regulation, if enforced, would weed out the bad apples, and we wouldn't be throwing the baby out with the bath water for the real value that affiliates offer the consumer.

Chairman WATT. Mr. Kittle, quickly though, because I have one other conflict that I want to clear up here.

Mr. KITTLE. Very quick is that you already have to disclose the affiliated business arrangement. That is disclosed, so I agree. But we are also required to give an approved provider list in addition to that which lists several closing services that the consumer can choose from. It was rightly said most of them don't choose to go anyplace else than what is recommended in 99 percent of the cases. So we already give an approved provider list in addition to the affiliated business arrangement.

Chairman WATT. I agree that most people do not look. In fact, I am just kind of in the position right now. I am refinancing. If I were refinancing in Charlotte, where I live, I know all of the providers. The title companies, the lawyers, the lenders, the brokers, I mean I would be shopping this thing to death. But closing a refinance of a condo here in Washington, I know none of the providers, so when I was offered the opportunity to just turn that over to somebody, it seemed like a good idea because I wasn't going to go take the time to shop around on this thing. So I mean I think it differs from market to market.

Mr. Savitt on this point.

Mr. SAVITT. Again, it is not the disclosure. I think everybody does disclosure properly. The problem here is the carrot that is dangled in front of the consumer: "If you use our settlement service providers you will receive a discount or an incentive, but if you do not use our service providers, you won't get the same discounts." So this is the problem. They are being coerced into using these specific settlement service providers and it is not always the best deal. As a matter of fact, the majority of time it is actually more expensive.

Chairman WATT. See, I thought this was the least controversial of the subjects.

A second issue that I wanted to see whether there was a way to reconcile was the opposing positions of Ms. Saunders and Ms. Borne and Mr. Kittle and Mr. Lindsey and Mr. Savitt, I believe, probably, on this whole YSP. Is there a way to reconcile your positions or are you all just—I take it that once I would like to just do away with yield spread premiums or some such—tell me how this can be reconciled. Mr. Savitt first, Mr. Kittle, and whomever else wants to weigh in, and then we are going to end this.

Mr. SAVITT. Well, the first thing I think we need to do is keep in mind the consumer here. This is all about the consumer. We have to level the playing field for consumer. We all talk about occasionally leveling the playing field for ourselves.

We have to level it for the consumer, and the way to do that is all originators, regardless of how they are licensed, should be required to disclose all of their direct and indirect compensation. Everybody discloses in the exact same form—or on the exact same forms in the exact same manner. This is what the FTC was talking about, because by making only brokers disclose their indirect compensation—and we know everybody gets it. As a matter of fact, that was addressed in 3915. Everybody gets it. So let's be fair to the consumer, let's have everybody disclose all of their indirect compensation in the exact same manner on the exact same forms, and then the consumer has a fighting chance.

Chairman WATT. Mr. Kittle.

Mr. KITTLE. Where we respectfully disagree with Mark and his group is, number one, yield spread premium disclosure is something that should remain. I think it is wrong to say, as we stated earlier, that every time you use yield spread premium or a broker that it results in higher costs to the consumer. That is absolutely wrong.

The individual loan officer company can set its own benchmark based on the price it receives from the lender, and they can determine to take less, and in many cases do in a competitive market, and reduce their cost and advertise an even lower rate with YSP. But as far as our difference here is, we think that it should be disclosed. People who are lenders, like myself, or larger members of the Mortgage Bankers Association, can't disclose what they are making on a loan in many cases—

Chairman WATT. But do you think the other costs ought to also be disclosed? If you are going to disclose yield spread premium for brokers, are there other internal costs if there is not an outside broker that also ought to be disclosed?

Mr. KITTLE. I think everything should be transparent. They are asking us to have a "level playing field." If I am going to hedge my loan, if I am going to portfolio that loan or hold it in my warehouse line, I can't tell you what I am making on it the day I close, whereas, when a broker closes the loan, their total compensation is received at that moment, on the spot.

Chairman WATT. Okay, I think the bottom line here is pretty much the same bottom line we got to on the other issue. If these things are done responsibly and they are disclosed and the buyer/consumer/borrower understands what is going on and it is of some benefit, then there is some value here. Is that a fair summary, Ms. Saunders?

Ms. SAUNDERS. Not quite, Mr. Chairman.

Chairman WATT. Give me a fair summary then.

Ms. SAUNDERS. We think disclosure in this instance is not sufficient. HUD clearly has under its statutory authority the authority to substantively regulate yield spread premiums, and we think that they should explicitly say yield spread premiums are legal only when they are the sole source of payment of the broker and all other fees. That way—

Chairman WATT. Can they do that in this rulemaking RESPA process or should that be a separate issue from the RESPA reform?

Ms. SAUNDERS. HUD has chosen in the years and years that it has been working on this effort to deal with yield spread pre-

miums. The consumer groups have consistently said both in the discussions, ongoing private and public discussions and in our comments that yield spread premium regulation needs to be substantive. There is no reason why that substantive regulation cannot be included in this rulemaking. It is part of RESPA. It is part of 2607 of RESPA.

Chairman WATT. Mr. Savitt, last word on this point. I am way over my time.

Mr. SAVITT. Okay, a couple of things. I have been saying this for a few years and it used to be a joke, but maybe it is not a joke anymore. Maybe we should rename RESPA the "Require Everyone to Show Profits Act." Mortgage brokers have been disclosing for 16 years everything they make, and we don't have a problem with that, but we think in order to be fair to the consumer, everybody should do it. Lenders know exactly what they are going to make on a loan, and I think it is also as to what Ms. Saunders said. It is allowable if all of the closing costs are included. Shouldn't this be the consumers choice whether they want to include all or part of their closing cost? We are taking choice away from the consumer if we follow her line of thinking.

Chairman WATT. My time has long since expired, and so I am going to treat you all the same way on this issue as I did Mr. Hinojosa.

We would welcome follow-up comments, written comments on this issue. I think these are the two major issues, really, where inside the panel there are disagreements. Generally speaking, the common thread through the panel was we don't like RESPA's rule in one respect or another, not always for the same reasons, but there was uniform opposition to immediate promulgation and finalization of a rule. But on these two issues we have some internal disputes in the panel.

Mr. Cleaver is recognized for 5 minutes.

Mr. CLEAVER. Thank you, Mr. Chairman. In fear that I would ask questions that have already been asked, I would just express appreciation to the panel, and I have surveyed your written comments. Thank you very much. If any of you have influence over HUD, would you please exercise it? Thank you.

[Laughter]

Chairman WATT. The gentleman yields back his time, and I would say to the gentleman and to all members that members may have additional questions for this panel which they may wish to submit in writing. Without objection, the hearing record will remain open for 30 days for members to submit written questions to these witnesses and to place their responses in the record.

It has been a wonderful hearing. The breadth and knowledge about this issue has been very impressive, the exact kind of input that we need in the legislative process. At this moment, this is outside the legislative process, but we reserve the right to pull it back in if it becomes necessary, and this might be an important predicate for doing that.

Let me do a couple of housekeeping things. I ask unanimous consent to submit for the record the following items. Number one, HUD's proposed rule that was issued in 73 Federal Register 14030–14061, dated March 14, 2008. Number two, the proposed

good faith estimate form. Number three, the existing good faith estimate form. Number four, an undated response letter to Representatives Hinojosa and Biggert from Sheila Greenwood. I think Mr. Hinojosa's unanimous consent request probably covered that. Number five, a statement for the record from the Independent Community Bankers of America dated September 16, 2008. I don't know how they didn't get on this panel, and they are probably mad at me, but I will make it up to them. Next, a statement for the record from the National Credit Reporting Association dated September 16, 2008. And—

Mr. MILLER. I would like to submit for the record a statement by Michele Bachmann.

Chairman WATT. A statement dated September 16, 2008, from Representative Michele Bachmann.

Without objection, those items will be submitted for the record.

Let me thank once again all of the witnesses for being here today to testify. It was a wonderful hearing, and the hearing is adjourned.

[Whereupon, at 11:56 a.m., the hearing was adjourned.]

A P P E N D I X

September 16, 2008

OPENING STATEMENT OF CHAIRMAN MELVIN L. WATT

SUBCOMMITTEE ON OVERSIGHT & INVESTIGATIONS

"HUD'S PROPOSED RESPA RULE"

TUESDAY, SEPTEMBER 16, 2008, 9:00 a.m.

Today's hearing is entitled "**HUD's Proposed RESPA Rule.**" The Real Estate Settlement Procedures Act of 1974 ("RESPA") is the federal statute that governs the mortgage settlement process for all Americans. As anyone knows who has ever bought a home or refinanced a home mortgage, the process involves most Americans' biggest investment and can be intimidating and complicated. Borrowers must sign dozens of forms and legal documents in one sitting, and quite often they do not understand everything (or anything) they are signing.

RESPA mandates the disclosure of certain terms, such as a home loan's initial interest rate, prepayment penalties and settlement costs, among others. RESPA and RESPA disclosures have been the subject of intense controversy and anticipated reform since at least the Reagan administration. The Financial Services Committee has held several hearings on RESPA

reform, most recently in the 105^{th} and 108^{th} Congress. Our colleagues on the Small Business Committee have also held hearings on RESPA reform, most recently this past May. RESPA reform continues to generate bipartisan interest and I thank the Ranking Member, Rep. Gary Miller, for requesting this hearing.

The reason for today's hearing is to examine the current proposed RESPA rule issued by HUD on March 14, 2008 for public for comment. At the outset, I should note that over 240 members of Congress have signed a "Dear Colleague" letter to HUD Secretary Steve Preston urging HUD to withdraw the proposed rule and commence a joint rulemaking with the Federal Reserve Board to produce more simplified mortgage and real estate settlement cost disclosure forms. The letter also warns that the proposed RESPA rule could hinder rather than help the recovery of the housing market, which is of even more concern in light of recent turbulence in the housing market and the government takeover of FANNIE MAE and FREDDIE MAC. Chairman Frank also wrote a letter to HUD Secretary Preston this past June urging HUD to work with the Federal Reserve Board to reconcile inconsistencies between the proposed RESPA and Truth-in-Lending Act (TILA) disclosure requirements to avoid consumer confusion

and redundant disclosures. I ask unanimous consent that the Members' letter dated August 7, 2008 and Chairman Frank's letter dated June 12, 2008 be made part of the record.

As one of the few members of the House who was neither a signatory to the letter from over 240 Members or to Chairman Frank's letter, I may be the only remaining Member of Congress who can truly be said to be publicly neutral on HUD's proposal. So I was glad when our Ranking Member requested the hearing. I thought it would be fun to see a bipartisan pummeling of a federal government agency and a spirited defense. I am always up for a good fiery discussion, if not a brawl. But alas, it's not going to happen. Before we could issue our invitation to HUD to come and explain what HUD was thinking, in August, HUD formally sent the proposed RESPA rule to the Office of Management and Budget for review and now claims that it is obliged not to further comment. So HUD Secretary Preston will not be with us today, despite our invitation. The Federal Reserve has also declined to testify, citing a reluctance to be critical of another federal agency in public. I would note however, that the Fed issued a staff comment letter dated June 13, 2008 expressing some concerns and I ask unanimous consent to submit that letter for the record.

We are pleased that representatives of virtually every other group I could think of have been lining up at the door to testify. We have a wide array of witnesses and we look forward to their testimony. It will be available to HUD and OMB for whatever use they desire to make of it.

At the end of the day, RESPA reform should be about improving disclosures to consumers so that they can understand their rights and responsibilities when buying a home and avoid unwelcome surprises at the settlement table. Perhaps the full brunt of the subprime crisis may have been avoided had consumers better understood what they were signing when buying a home. At the same time, RESPA reform should not unnecessarily confuse consumers, nor result in unreasonable regulatory burdens and costs to the real estate industry as the fragile housing market seeks a recovery. In any event, under the Congressional Review Act, 5 U.S.C. § 801, Congress has the opportunity to review an agency rule before it can take effect, and we reserve the right to do so. I will now recognize the Ranking Member for his opening statement.

Statement by Rep. Michele Bachmann
Oversight and Investigations Subcommittee
Hearing on HUD's Proposed RESPA Rule

September 16, 2008

Thank you, Chairman Watt, for holding this important hearing on the U.S. Department of Housing and Urban Development's (HUD) proposed rule regarding the Real Estate Settlement Practices Act (RESPA).

This proposed rule has been the cause of great concern for many of my constituents – from homebuyers and mortgage bankers to realtors and community bankers. All share similar concerns that HUD's rule will do more harm than good – that the proposal will only further burden homebuyers with confusing, unnecessarily complicated, and inconsistent terms about their loans and settlement costs. Most agree that this rule will impose serious new costs on the mortgage industry at a time when it is already suffering tremendous turmoil in the housing marketplace.

I hold similar concerns and that is why I joined 244 of my colleagues in sending a letter to HUD asking for an additional extension of the comment period for this proposed rule. This would ensure HUD, industry stakeholders and consumers have adequate time to evaluate this proposal. We were successful in securing a thirty day extension and it now remains to be seen what real improvements will be made.

While HUD has the responsibility to administer RESPA and ensure consumers' receive good faith disclosures of their closing costs, the Federal Reserve Board has jurisdiction over the Truth in Lending Act (TILA) which governs the terms of mortgage loans. Currently, the Fed is working to update TILA disclosure requirements through what we all know as "Regulation Z." It is unclear why HUD has not more closely worked with the Fed so that these regulatory updates may complement, not clash with, one another.

We do not yet know what changes have been made to the proposed rule which is currently under examination by the Office of Management and Budget (OMB). However, I believe that through hearings such as today's we can continue to ease marketplace concerns with the hope that HUD will produce a more cohesive, workable rule that benefits all parties. Our nation is experiencing a period of turmoil in the housing market and perhaps now more than ever, it is imperative that Americans receive full, simplified disclosure of the terms of their real estate settlements.

I appreciate the witnesses coming before the committee today and look forward to this important discussion.

Testimony of Rebecca Borné
Center for Responsible Lending

Before the U.S. House of Representatives
Committee on Financial Services
Subcommittee on Oversight and Investigations

"HUD's Proposed RESPA Rule"

September 16, 2008

Chairman Watt, Ranking Member Miller, and members of the Subcommittee, thank you for holding this hearing on HUD's Proposed RESPA Rule and for inviting us to testify.[1] HUD should be commended for its proposal to reform RESPA, which represents a significant step forward. However, before finalization, HUD should address several important deficiencies in its proposal, both disclosure-related and substantive. Most critically, HUD should use its authority under RESPA to eliminate a key driver of the foreclosure crisis: abusive yield-spread premiums.

I am Policy Counsel at the Center for Responsible Lending (www.responsiblelending.org), a not-for-profit, non-partisan research and policy organization dedicated to protecting homeownership and family wealth by working to eliminate abusive financial practices. CRL is an affiliate of Self-Help (www.self-help.org), which consists of a credit union and a non-profit loan fund. Self-Help is a relatively small lender that must comply with RESPA. While HUD's Proposed Rule should do more to protect consumers, we believe its provisions, and any recommended changes we have made to them, are administratively feasible for both larger and smaller lenders.

For the past 28 years, Self-Help has focused on creating ownership opportunities for low-wealth families, primarily through financing home loans to low-income and minority families who otherwise might not have been able to get purchase homes. In other words, we work to provide fair and sensible loans to the people most frequently targeted for predatory and abusive subprime mortgages. Self-Help has provided over $5 billion in financing to more than 60,000 low-wealth families, small businesses and nonprofit organizations in North Carolina and across the United States. Although Self-Help is technically a subprime lender, its responsible lending practices have kept its annual loan loss rate under one percent—far less than the typical subprime loss rate.

In addition to making direct loans, Self-Help encourages sustainable loans to applicants with blemished credit through a secondary market operation, which we have used to provide financing to thousands of families across the country—loans that have performed well and increased these families' wealth.

Today, as the U.S. economy faces significant challenges, the need to ensure a transparent accounting of costs in real estate transactions has become clearer than ever. Right now, it is estimated that at least 20,000 foreclosures on subprime mortgages are taking place every single week.[2] The negative spillover effects from these foreclosures are substantial: a single foreclosure causes neighborhood property values to drop, collectively adding up to billions of

dollars of losses. Empty homes lead to higher crime rates. Lost property tax revenue hurts cities and counties that are already strapped. Millions of Americans who depend on a robust hosing market are losing jobs and income. As foreclosures accelerate during the next two years, these economic effects will be felt even more strongly.

Confusing, misleading, and inaccurate information has played a contributory role in the current mortgage crisis, and reforms to the current disclosure requirements are long overdue. We commend the staff of HUD for its diligent work in crafting this proposal. We recognize that the home mortgage process is unique and complex and that developing a fair and reasonable method of ensuring early and accurate price disclosure is challenging. HUD has done a tremendous amount of work to develop a proposal that represents some important improvements over existing requirements—it offers a standardized shopping tool with better linkages to the HUD-1, requires that some terms be binding, and requires improved disclosures aimed at alerting borrowers to the risky features of their loans. HUD should be congratulated for this effort.

We cannot overemphasize, however, that poor disclosure has not been the driver of the foreclosure crisis. It has been only part of a broader system of skewed incentives that have encouraged mortgage originators to steer consumers into the riskiest, highest-cost loans available. Brokers could wash their hands clean of these loans as soon as they collected their origination fees, and lenders could do the same as soon as they sold them off into the secondary market.

Lender-paid fees to brokers, or yield-spread premiums, played an integral role in this system of skewed incentives—a role that RESPA, by its statutory language alone, should not have allowed them to play. HUD has the authority and the responsibility, as the enforcing agency of RESPA, to recognize that under certain circumstances, yield-spread premiums violate the illegal kickback provisions of §8 of RESPA. Such recognition would be consistent with the purpose of the statute: *to ensure that consumers are protected from unnecessarily high settlement charges caused by abusive practices.*[3] And such recognition would be the single most helpful change HUD could make through RESPA because it would get to the real heart of the problem: a broken market, with broken incentives, that no disclosure—no matter how clear—will repair.

We further emphasize that even within the realm of disclosure, RESPA does not represent nearly the complete picture. RESPA governs disclosure of settlement costs, while the Truth in Lending Act (TILA) governs cost of credit disclosures that provide the bottom-line price tag for the loan. Settlement costs and finance costs are interdependent, and manipulation of the relationship between the two is a common way consumers have been tricked into abusive loans. Therefore, HUD should coordinate with the Federal Reserve Board to develop a comprehensive disclosure system that allows consumers to shop based on the entire cost of the loan. Short of coordination with the Federal Reserve, HUD should nonetheless design a Good Faith Estimate (GFE) that tries to alert consumers to the risky features of their loan. HUD's proposed GFE does this more effectively than what is currently required, but as we discuss later in this testimony, it should go further.

It's also critical to understand that RESPA disclosures do little for those consumers who are not in fact shopping independently. Most victims of predatory lending did not go out shopping for

loans; rather, loans were push-marketed to them by people marketing their expertise, but who were in fact promoting not a loan with the interest rate and terms the consumer qualified for, but the *most expensive* loan. The most expensive loan earned the broker the most in kickbacks from the lender—kickbacks that are allowed only because HUD has not used its authority under RESPA to ban them.

In short, RESPA disclosures are no solution to predatory lending. Whatever decisions are made with respect to the disclosures in this Proposed Rule will not prevent future predatory loans from being made. They will not fix the misaligned market incentives that created this mess.

We understand that many in industry have called for the Proposed Rule to be withdrawn. We have not joined that petition in recognition that the Rule does represent important strides forward, and, with recommended improvements, could achieve real progress with respect to disclosure. HUD should not be asked to start from square one and completely overhaul its Proposed Rule. However, we also recognize that once final rules are issued, we may not see further RESPA reform for a very long time, and, if not done correctly, this iteration may stand as a lost opportunity. To ensure that this reform is worthwhile, HUD's proposed improvements should be enhanced by addressing several critical deficiencies in the Proposed Rule:

1. Eliminate yield-spread premiums that do not offer benefits to consumers;

2. Coordinate with the Federal Reserve Board to develop a single form that complies with RESPA and TILA;

3. Request Congressional action to provide adequate enforcement mechanisms, including a private cause of action, to ensure that RESPA does what it's meant to do;

4. Require an interest rate lock to allow consumers to meaningfully compare loan costs;

5. Avoid authorizing fees for the GFE because fees will create barriers to shopping for consumers;

6. Ensure that the GFE facilitates consumers' ability to understand the riskiest features of their loans, particularly by (i) increasing emphasis on the monthly payment; (ii) requiring disclosure of the APR; (iii) requiring disclosure of the first date the interest rate can rise; (iv) and disclosing broker compensation in a simple, straightforward manner;

7. Add protections to the closing script requirements; and

8. Update RESPA's servicing rules to better protect homeowners.

I. LAYING THE FRAMEWORK: MISALIGNED INCENTIVES AND PREDATORY LENDING HAVE CAUSED THIS FORECLOSURE CRISIS, SPURRING A NATIONAL AND INTERNATIONAL CRISIS AS WELL.

Just over a year ago, some in the mortgage industry were still insisting that the number of foreclosures would be too small to have a significant impact on the economy overall.[4] No one makes that claim today. As foreclosures reach an all-time high and are projected to grow higher,[5] the "worst case is not a recession but a housing depression."[6] At least two million American families are expected to lose their homes to foreclosures initiated over the next two years.[7] Industry projections forecast that by 2012, 1 in 8 mortgages—that's all mortgages, not just subprime mortgages—will fail.[8]

As we show in our recent report on the spillover effect of subprime foreclosures, the consequences of foreclosures are not confined to the families who lose their homes. Forty million of their neighbors will see their property values decline by over $350 billion.[9] Federal Reserve Chairman Ben Bernanke recently noted:

> At the level of the individual community, increases in foreclosed-upon and vacant properties tend to reduce house prices in the local area, affecting other homeowners and municipal tax bases. At the national level, the rise in expected foreclosures could add significantly to the inventory of vacant unsold homes—already at more than 2 million units at the end of 2007—putting further pressure on house prices and housing construction.[10]

Robert Schiller recently noted that the meltdown and resulting crisis has erased any gains in the homeownership rate made since 2001, and the rate stands to fall further yet.[11] Even more ominous, according to the IMF, direct economic losses stemming from this crisis will likely top $500 billion and consequential costs will total close to a trillion dollars.[12]

It's not very hard to imagine how costs could get that high. Major banks and investment firms have already collapsed, and others appear not far behind. In March, Bear Stearns, after receiving an unprecedented emergency loan from the Federal Reserve, was purchased by JP Morgan for $10 a share, its stock-market value having plummeted to $3.5 billion from over $20 billion just over a year earlier.[13] In July, IndyMac was placed into conservatorship by the FDIC, representing one of the largest bank failures in U.S. history. On September 7, Fannie Mae and Freddie Mac were placed under conservatorship by the U.S. Treasury. And as this testimony was being written, the Treasury Department and the Federal Reserve were reportedly planning to assist in a sale of the badly struggling Lehman Brothers.[14]

This pervasive crisis may not have occurred if borrowers had simply been given the type of loan that they qualified for. Last year, the Wall Street Journal found that of the subprime loans originated in 2006 that were packaged into securities and sold to investors, 61% "went to people with credit scores high enough to often qualify for conventional [i.e., prime] loans with far better terms."[15] Even those applicants who did not qualify for prime loans could have received sustainable, thirty-year, fixed-rate loans for—at most—50 to 80 basis points above the "teaser rate" on the unsustainable exploding ARM loans they were given.[16] Indeed, many consumers

were charged 100 basis points more for "no-doc" loans when they had already handed over their W-2 statements or readily would have done so but for the broker's desire to originate these riskier loans.[17] That made the typical risky adjustable rate subprime loan more expensive than far safer thirty-year fixed-rate loans *even at the initial payment.*

Wall Street's appetite for risky loans incentivized mortgage brokers and lenders to aggressively market these highly risky ARM loans instead of the sustainable loans for which consumers qualified. As Alan Greenspan told *Newsweek*:

> The big demand was not so much on the part of the borrowers as it was on the part of the suppliers who were giving loans which really most people couldn't afford. We created something which was unsustainable. And it eventually broke. If it weren't for securitization, the subprime loan market would have been very significantly less than it is in size.[18]

Market participants readily admit that they were motivated by the increased profits offered by Wall Street in return for risky, higher-yielding loans. After filing for bankruptcy, the CEO of one mortgage lender explained it this way to the New York Times, "The market is paying me to do a no-income-verification loan more than it is paying me to do the full documentation loans," he said. "What would you do?"[19] Even the chief economist of the Mortgage Bankers Association, when asked why lenders made so many unsustainable loans, replied, "Because investors continued to buy the loans."[20]

In short, this crisis was primarily caused by loan originators selling unnecessarily risky loans to homeowners who did not understand what they were getting into, either because they were affirmatively misled or because the information they were given was simply too complex and voluminous. A primary role of RESPA reform should be to make such steering less likely by providing consumers with clear and concise information that will help them better understand their mortgage options.

Even improved disclosure, however, will not provide sufficient protection to consumers dealing with complex mortgage transactions, particularly when they are subjected to inherently abusive practices encouraged by a broken incentive structure. HUD's effective blessing of incentives that encourage steering consumers to unaffordable loans only makes the situation worse. *Only substantive reform, in addition to improved disclosures, can adequately protect consumers, curb abusive lending practices, and restore health to the market.*

II. SPECIFIC RECOMMENDATIONS

1. Eliminate yield-spread premiums that do not offer benefits to consumers.

One of the primary concerns we have with the proposed GFE is its misleading disclosure of yield-spread premiums. We discuss these concerns in section 6, below. However, the most important point we hope to convey through our testimony is this: *Yield-spread premiums are more effectively and appropriately addressed substantively under RESPA's §8 than through disclosure.*

HUD holds to the position that the option to pay some closing costs through the rate should be available, but it also states that it "should be at the consumer's choice, based upon a complete understanding of the trade-off between up-front settlement costs and the interest rate."[21] As we explain in section 6, the proposed GFE falls short of providing the information necessary for an informed choice, and it simply cannot ensure that such a trade-off exists.

HUD's policy position on YSPs rests on two key points: (1) they can be a useful option to help pay some or all closing costs through the higher rate rather than financing them in the loan or paying cash upfront;[22] however, (2) payment solely for delivering a higher-cost loan to a lender is not a compensable service.[23] Unfortunately, empirical evidence now confirms that in the subprime, Alt-A, and FHA sectors, YSPs are often in exchange for exactly that—a higher cost loan, made so by a higher interest rate, no documentation, or a prepayment penalty.[24]

The irony with respect to prepayment penalties, of course, is that the public justification for them was that they were a price-trade-off that would result in a *lower* interest rate. Few consumers would knowingly choose to simultaneously pay a "rate-increasing" YSP and a "rate-reducing" prepayment penalty. Yet the subprime market was filled with loans with prepayment penalties and YSPs.[25]

Dr. Susan Woodward's recent study of FHA loans found that, except in the instance of true "no-cost" loans, YSPs are associated with higher, not lower costs. The net loss to those who pay YSPs ranges from $93 per $100 of YSP paid for brokered loans to $71 per $100 of YSP paid for mortgage bank loans.[26] Another study, released in 2007, showed that consumers only receive 25 cents in reduced fees for every one dollar paid in YSPs to brokers and that upfront fees are actually lower for retail loans than for brokered loans.[27] CRL released a study earlier this year that dramatically demonstrated the dichotomy between the prime and subprime markets.[28] The evidence from that study (which could not isolate settlement costs) indicates that brokers in the prime market may help consumers find the cheapest deal, but that this is not the case in the subprime market. Brokered loans, when compared to direct lender loans, cost subprime borrowers additional interest payments ranging from $17,000 to $43,000 per $100,000 borrowed over the scheduled life of the loan. Even over a fairly typical four-year loan term, the subprime consumer pays over $5,000 more for brokered loans.[29]

Among the most important—although unsurprising—findings of both the Federal Trade Commission study of homeowners' understanding of mortgage terms and Dr. Woodward's study was that consumers have more trouble understanding complex loan terms.[30] It appears as though, in working with the focus groups on the proposed GFE, HUD resolved this quandary by designing a disclosure that assumes that "all else would be equal" in weighing the trade-offs. While that certainly makes for more streamlined disclosures, it does not change the fundamental problem. It only simplifies the disclosure—not the product, not the choices, and not the economic consequences of those choices. Assuming away complexity will not result in the "complete understanding" of the trade-offs that is HUD's stated goal in its disclosure proposal regarding YSPs. In reality, it is virtually impossible to disclose a way through the minefield of multiple terms layering impacts on the rate.

Fortunately, RESPA is not solely a disclosure law. Indeed, a cornerstone of the law is the prohibition against fees for referrals or otherwise unearned fees under §8.[31] In enacting RESPA, Congress recognized that anti-competitive behavior, and unearned compensation, made the already expensive mortgage even more expensive. It adopted a combination approach—disclosure plus substantive regulations taking square aim at anti-competitive, market-distorting conduct. By simply providing strict conditions to ensure that YSPs are in fact an "alternative" way to pay costs, rather than simply a reward to brokers for delivering loans with higher costs or riskier terms, HUD would give flesh to §8's intent to prohibit anti-competitive and costly market perversions.

In other contexts, we have recommended to regulators and legislators that YSPs be categorically prohibited in the subprime and non-traditional segments of the market, since experience and evidence demonstrate that YSPs do not result in a price trade-off in those segments. To the extent RESPA encompasses authority to make such a distinction, we would similarly urge a specific rule stating that §8 bans YSPs in those segments.[32] But where allowed at all—whether just in the prime market, or in all markets if HUD does not ban YSPs in the subprime and non-traditional markets—it is necessary that HUD use the power RESPA already provides it to fix this broken system. Under existing RESPA §8 provisions, prescribing a set of specific conditions as to when YSPs are permitted is well within HUD's authority, carries out the letter and spirit of the law, will curb the abuses where they exist, will not adversely affect the portions of the market where they do not, and, finally, will assure that the promised price trade-offs actually occur. We therefore recommend that the relevant portion of 24 CFR §3500.14 be amended to read:

> A yield-spread premium, or similar charge however denominated, may be permitted as *bona fide compensation* for services actually performed only where:
>
> (A) the mortgage broker receives no other compensation, however denominated, directly or indirectly, from the consumer, creditor, or other mortgage originator;
> (B) the loan does not include discount points, origination points, or rate reduction points, however denominated, or any payment reduction fee, however denominated;
> (C) the loan does not include a prepayment penalty; and
> (D) there are no other closing costs associated with the loan, except for fees to government officials or amounts to fund escrow accounts for taxes and insurance.

We note that one state, Massachusetts, recently enacted regulations which effectively prevented originators from using YSPs as a mechanism for self-rewards, although it was accomplished in a different way.[33] The reform does not appear to be restricting access to responsible credit in the state.[34] HUD should step to the forefront nationally and enact similar regulations.

We also note that the Federal Reserve Board, in its most recent amendments to Regulation Z, attempted to address YSPs through disclosure alone. It ended up withdrawing that part of its proposal after consumer testing demonstrated that consumers did not understand YSPs at all and that the proposed disclosure did not necessarily lead consumers to choose the cheapest loan. It has committed, as it continues its comprehensive review of Regulation Z, to "consider whether

disclosures *or other approaches* could effectively remedy this potential unfairness [caused by YSPs]" (emphasis added).[35]

2. **Coordinate with the Federal Reserve Board to develop a single form that complies with RESPA and TILA.**

Coordination between HUD and the Federal Reserve Board to develop a single disclosure form is long overdue. While HUD disclosures relate to settlement costs and the Federal Reserve Board disclosures relate to the cost of credit, the two types of costs are inextricably intertwined. Consumers should be able to evaluate all cost factors together in order to see the whole picture and make the most informed choice possible.

The proposed GFE includes several disclosures that overlap with related, but not identical, TILA disclosures, which may be very confusing to consumers. For example, the proposed GFE includes only principal, interest, and mortgage insurance in the monthly payment disclosure, while TILA also allows creditors to include taxes and homeowners' insurance in the monthly payment disclosure. The proposed GFE includes the "initial loan balance," while the "amount financed" included in TILA disclosures will be different if, as is common, the prepaid finance charges are financed as part of the loan. The proposed GFE requires the initial note rate while TILA requires the APR. HUD plans to use its Special Information Booklet to explain differences between the GFE and TILA,[36] but consumers are unlikely to read and process all four pages of the proposed GFE, much less an accompanying booklet. The two agencies should coordinate to develop one integrated form.

3. **Request Congressional action to provide adequate enforcement mechanisms, including a private cause of action, to ensure that RESPA does what it's meant to do.**

RESPA violations are notoriously underenforced at this time. Consequently, we were glad to see that HUD plans to ask Congress to provide for civil penalties, injunctive relief, and equitable relief for several sections of RESPA. However, unless a private right of action and the possibility of actual damages also exist for all sections of RESPA, enforcement will continue to be minimal and RESPA violations will continue to be rampant throughout the industry. Given the volume of mortgage lending in this country, there will never be sufficient public resources to rely solely on public enforcement.

Therefore, we urge that Congress add a private cause of action to RESPA, especially with respect to the HUD-1 and GFE, by codifying that the violation of those provisions constitutes an unfair trade practice, as some states have done. Absent the availability of a private cause of action, relief to consumers taken advantage of by abusive lending practices is rarely obtained.

4. **Require a longer binding period and an interest rate lock to allow consumers to meaningfully compare loan costs.**

The 10-day period HUD has proposed for which the GFE must remain binding is remarkably short. A 30-day binding period would be far more reasonable. Many consumers will not have the flexibility within a 10-day period to gather a sufficient number of loan quotes. As a result, they will find themselves paying for multiple GFEs from the same originator because their 10-day guarantee period has run out. In addition, originators should easily be able to project settlement costs at least 30 days in advance.

The most striking problem with the 10-day period is that, despite being so short, it does not apply to the interest rate, which can come with no guarantee at all. HUD absolutely must require an interest rate lock in order for the GFE to be effective. Without a rate lock, consumers must shop on settlements costs alone, which are a relatively small component of total lost. It is also easy for originators to bait and switch consumers by presenting deceivingly low settlement costs, only to recoup those costs by increasing the rate when the consumer comes back a few days later. The large majority of prime rate lenders offer a *30-day* interest rate lock, which indicates that (1) the implementation cost of a required rate lock would be minimal; and (2) a 10-day rate lock is more than feasible.

5. **Do not explicitly authorize fees for the GFE because fees will create barriers to shopping for consumers.**

An essential element of effective shopping is the ability to obtain multiple loan quotes. The cost of obtaining multiple GFEs will add up to a significant total for many consumers and will discourage consumers living on the margin from obtaining more than one quote. In addition, we are concerned that the costs of completing the HUD-1 and TILA disclosures, which are prohibited from being passed along to consumers, will be slipped through to consumers instead as a "GFE fee." Some states have recognized the negative impact nonrefundable application fees have on consumers and prohibit them by law. In the interest of consumers and their access to shopping, HUD should at least remain silent on whether GFE fees may be charged, and it should by no means endorse it.

6. **Ensure that the GFE facilitates consumers' ability to understand the riskiest features of their loans, particularly by (i) increasing emphasis on the monthly payment; (ii) requiring disclosure of the APR; (iii) requiring disclosure of the first date on which the interest rate can rise; and (iv) disclosing broker compensation in a straightforward manner.**

We commend HUD for the extensive consumer testing it performed on numerous variations of the GFE. We understand that HUD may be hesitant to make changes to its proposed GFE given that extensive testing. However, we strongly encourage HUD to consider our recommendations in light of three limitations of its testing—the first a universal limitation, the second unique to the current mortgage market, and the third specific to HUD's approach. First, individuals respond differently when they know they are being tested than when they are not being tested. For example, a test subject may read long forms while being watched, while in a real-life transaction,

these forms may be rarely read. Second, many originators, especially those who do not hold on to the credit risk of their loans, have a financial incentive to encourage consumers to ignore most of the GFE. Third, HUD's testing did not consider one crucial, slippery feature of loan pricing: the relationship between settlement costs and interest rate.

(i) *The GFE should include all components of the monthly payment on page one.*

The vast majority of consumers shop for a mortgage focusing not on rates, settlement costs, or other loan features, but on the one key number that signals to them whether or not they can afford the loan: the grand total that they will have to pay each month for their home.

Unscrupulous lenders fully understand the desire to shop based on monthly payment, which explains why a primary way they sell abusive loans is to artificially deflate the monthly payment through teaser rates, discount points that don't provide a fair rate trade-off, and prepayment penalties. In addition, many lenders do not require borrowers to escrow for property taxes and insurance, which makes the monthly total appear very low in comparison to totals that include the full PITI. This deception has been particularly useful for lenders seeking to refinance people out of an existing loan into a loan that looks cheaper because the homeowner is currently escrowing, but in reality is much more expensive.

We applaud HUD's inclusion of the initial monthly payment and the maximum monthly payment of principal, interest, and mortgage insurance on page one of the GFE. We further commend HUD for including Total Other Annual Charges (property taxes, homeowners insurance, flood insurance, homeowner association/condominium fees) in the proposed GFE. We are concerned, however, that consumers will not consider them when weighing whether or not they can afford the loan because they are buried on page four. While we understand that these costs are not relevant to comparison shopping because they are not determined by the originator, they are nonetheless vital to determining affordability. Therefore, we suggest that the additional charges total be displayed on page one, as well as the sum of additional charges and the maximum monthly payment.

(ii) *The GFE must include the Annual Percentage Rate (APR) and reduce its disproportionate focus on settlement costs.*

Ideally, of course, HUD and the Federal Reserve Board should coordinate and develop a single disclosure form. Short of that, however, the APR is still the better rate to disclose on any shopping document. We understand that with its proposed GFE, HUD is attempting to allow shopping for settlement costs while holding the note rate constant, rendering the APR irrelevant. The APR is far from perfect. However, it is the one single price that captures all finance charges, whether upfront or charged over time. It also potentially reduces the deception caused by teaser rate loans because it is a composite rate, reflecting both the initial low rate and the future increased rate. As a result, it could help consumers comparison shop between a fixed rate mortgage from one lender and an adjustable rate mortgage from another.

In addition, HUD's attempt to allow shopping based on settlement costs alone while holding the note rate constant is unlikely to play out in real life. Consumers may end up with three GFEs

containing three different note rates, three different monthly payments, three different amortization schedules, and three different settlement cost amounts. In this case, the only apples-to-apples comparison is the APR.

(iii) *The GFE must disclose the first possible date on which the interest rate can rise.*

In most types of adjustable rate loans, an increase in the monthly payment will follow an increase in the interest rate. Where it does not, as in payment option ARMs, it is still important that the consumer understand that the typically very low initial interest rate will likely last a very short time, usually just a few days or weeks. Therefore, the GFE must disclose the first possible date on which the interest rate could rise, both to warn consumers when they should be prepared to meet a higher monthly payment obligation and to alert them to the fact that some "teaser rates" are extremely ephemeral.

(iv) *Broker compensation should be disclosed in a simple and straightforward manner.*

In Section 1 above, we discuss the broader skewed incentives created by YSPs and explain why we believe they are illegal kickbacks in certain contexts. Apart from the need for substantive reform, the disclosure is misleading and must be replaced with a simpler disclosure even if substantive reforms are not made.

We appreciate HUD's effort to try to make the disclosure of broker fees more transparent. YSPs, and rate/point trade-offs in general, are so complex that disclosing them clearly is very difficult. We understand that one aim of HUD's disclosure was to avoid disadvantaging brokers relative to lenders. However, incentives driving the way brokers price loans are not equal to those driving lenders, so HUD's desire to treat the origination fees paid to each the same is not justified.[37] Moreover, as noted earlier, empirical evidence suggested brokered loans in the subprime market cost consumers significantly more than direct lender loans.[38]

There are several problems with the proposed disclosure. First and foremost, it *presumes* a trade-off for the consumer through a reduction in upfront costs, although the evidence is that such a presumption is not warranted. We understand that HUD believes that the "Looking at trade-offs" table on page three provides protections for consumers. However, it only ensures a fair trade-off in an environment of fixed and transparent pricing, which is not the reality of the subprime market. Consumers don't see originators' rate sheets. Originators could easily inflate the base rate and fill out the entire table, making it appear that the consumer is getting a fair-trade off—when in fact the same incentives are driving the same abusive practices and the consumer is still paying a higher interest rate than he or she qualifies for.[39]

Second, the disclosure's characterization of the YSP as a "credit" suggests that this arrangement is somehow saving the customer money, when it is in fact doing just the opposite. This nomenclature could even end up advantaging brokers over lenders, while seriously misleading prospective homebuyers.

Third, the disclosure in no way makes clear that this is a fee paid to a broker. It never uses the word "broker" and tells the consumer nothing about the dynamic at play among the broker, the lender, and the consumer's loan costs. There would be some value derived from the sheer "sticker shock" that occurs when a consumer realizes how much the total broker fee is in an abusive loan.

We recommended that the following more simple, straightforward, and honest disclosure replace number 2 on the top of page two. This disclosure breaks out the portion of the broker fee paid directly by the consumer and the portion paid by the lender and recouped from the consumer through a higher interest rate:

MORTGAGE BROKER COMPENSATION	
Mortgage Broker Fees paid by you directly (included in settlement charges):	$
+ additional fee received by broker from lender and paid by you through increased loan interest rate:	$
Total Broker Fees:	**$**

7. Add protections to the closing script.

Given the extensive damage wrought to the international economy by the failure of lenders to explain highly complex loans to consumers, a clear, oral explanation of the loan seems both obvious and crucial. We commend HUD's efforts, and we agree that the opportunity for consumers to hear an oral explanation and ask questions is more effective than being handed a stack of forms with no discussion. Without additional protections, however, the risks entailed by this closing script may outweigh the benefit of providing an oral explanation to the consumer at settlement.

First, there is the possibility that closing agents or settlement attorneys might fail to read through the closing script in a meaningful way that adds to the consumer's understanding. Second, the agent or attorney might fail to read it at all, yet the consumer might still unwittingly sign it as part of the barrage of other signatures required at closing or might be persuaded to sign it as just another "meaningless government form."[40] (In fact, this almost assuredly will happen frequently, as hurried closings are often part of a strategy for pushing unsuitable loans.[41]) Third, the agent or attorney themselves might not fully read through the loan documents and therefore provide the consumer with incorrect information received from the lender. Fourth, the existence of the signature might be used in court as evidence that the consumer understood the loan, even if that is not the case.

If this script is to be required, we strongly recommend that it does not have a consumer signature requirement. Alternatively, the rules should clarify that the consumer's signature is not conclusive evidence that the disclosures were made. In addition, the script must disclose and explain the APR as the price which includes both interest and fees. It must also prominently

disclose the consumer's three-day right to rescind for non-purchase money mortgage transactions.

Finally, HUD should clarify that the consumer has the right to rely on the accuracy of the closing script and that the lender is jointly liable for any inaccuracies in it.

8. Update RESPA's servicing rules.

The current foreclosure crisis has made clear the critical role servicers play once loans become delinquent. Often it has been the servicer that ultimately determines whether or not a consumer ends up with an affordable loan modification. RESPA's servicing rules should be updated (i) to require that servicers engage in reasonable loss mitigation prior to foreclosure; (ii) to prohibit broad release language in modifications or forbearance agreements that cuts off borrower's past and future claims against the servicer or holder; and (iii) to shorten the period of time a servicer has to respond to a borrower's Qualified Written Request from 60 days to 14 calendar days. For further discussion of these requirements, see the National Consumer Law Center's Comments on the Proposed Rule.[42]

We note that improved servicing protections are incorporated in H.R. 5679, The Foreclosure Prevention and Sound Mortgage Servicing Act of 2008, introduced by Chairwoman Waters, which we have endorsed.

CONCLUSION

In conclusion, we applaud HUD for addressing the challenge of reforming RESPA. We believe HUD's proposed GFE provides important improvements over existing requirements, but we do not think it should be finalized without incorporating our suggested changes aimed at alerting consumers to the riskiest features of their loan, particularly with respect to the broker compensation disclosure.

In addition, we remain convinced that there are some financial incentives so strong and so skewed that they create problems disclosures cannot fix. In fact, these incentives undermine most of what HUD hopes to accomplish through this Proposed Rule. We know that HUD shares our commitment to protect consumers, as recently conveyed by RESPA Director Ivy Jackson: "It is no longer acceptable to stand in the way of millions of Americans who are crying out for clarity when it comes to the biggest purchase of their lives."[43] As noted earlier, lack of clarity is not due to poor disclosure as much as it is due to complex loan terms driven by warped incentives that encourage minimal transparency in the mortgage market. This minimal transparency cannot be overcome even by the clearest of disclosures. We hope that HUD will make the substantive reform needed to correct this broken market and give consumers the clarity they deserve.

We look forward to continuing to work with HUD in its efforts. We appreciate the Subcommittee's interest in RESPA reform, and we are happy to answer any questions.

[1] Real Estate Settlement Procedures Act (RESPA): Proposed Rule To Simplify and Improve the Process of Obtaining Mortgages and Reduce Consumer Settlement Costs, 73 Fed. Reg. 14030-124 (March 14, 2008) (hereafter "Proposed Rule").

[2] *See* Written Testimony of Mark Zandi, Moody's Economy.com, before House Subcommittee on Commercial and Administrative Law (Jan. 29, 2008), *available at* http://judiciary.house.gov/hearings/pdf/Zandi080129.pdf (hereafter "Zandi Testimony"); *see also* Center for Responsible Lending, *Subprime Spillover* (Rev. Jan. 18, 2008), *available at* http://www.responsiblelending.org/issues/mortgage/research/subprime-spillover.html (hereafter "*Subprime Spillover*").

[3] 12 C.F.R. §2601 (emphasis added).

[4] *See, e.g.*, Statement of John M. Robbins, CMB, Chairman, Mortgage Bankers Association, at the National Press Club's Newsmakers Lunch – Washington, DC (May 22, 2007) (Speaking of predicted foreclosures, Mr. Robbins stated: "As we can clearly see, this is not a macro-economic event. No seismic financial occurrence is about to overwhelm the U.S. economy."); Julia A. Seymour, "Subprime Reporting, Networks blame lenders, not borrowers for foreclosure 'epidemic,'" Business & Media Institute (Mar. 28, 2007) ("[T]here are experts who say the subprime 'meltdown' is not the catastrophe reporters and legislators are making it out to be. 'We don't believe it will spill over into the prime market or the U.S. economy,' said [Laura] Armstrong [Vice President, Public Affairs] of the Mortgage Bankers Association").

[5] Renae Merle, *Home Foreclosures Hit Record High*, Washington Post (Mar. 6, 2008).

[6] David M. Herszenhorn and Vikas Bajaj, *Tricky Task of Offering Aid to Homeowners*, N.Y. Times (Apr. 6, 2008) (quoting Susan M. Wachter, a real estate finance professor at the Wharton School of the University of Pennsylvania: "In the market that we have in front of us, prices decline and supply increases, driving prices down further.").

[7] *See* Zandi Testimony, *supra* note 2; *Subprime Spillover*, *supra* note 2.

[8] Rod Dubitsky, Larry Yang, Wen Zhang and Thomas Suehr, *Foreclosure Trends – A Sobering Reality*, Credit Suisse, Fixed Income Research (Apr. 28, 2008).

[9] See Center for Responsible Lending, The Impact of Court-Supervised Modifications on Subprime Foreclosures, (Feb. 25, 2008), *available at* http://www.responsiblelending.org/pdfs/us-info-with-fc-starts.pdf; for CRL's methodology for computing spillover, *see Subprime Spillover*, *supra* note 2.

[10] Statement of Federal Reserve Chairman Ben Bernanke on March 4, 2008, reprinted by Bloomberg.com, *available at* http://www.bloomberg.com/apps/news?pid=newsarchive&sid=apeU.0IaETdM.

[11] Robert J. Schiller, *The Scars of Losing a Home*, N.Y. Times (May 18, 2008) (noting that the homeownership rate has fallen from 69.1% in 2005 to 67.8% in the first quarter of 2008, nearly the 67.5% rate at the beginning of 2001).

[12] Christopher Swann, *IMF Says Financial Losses May Swell to $945 Billion,* Bloomberg.com (Apr. 8, 2008), *available at* http://www.bloomberg.com/apps/news?pid=email_en&refer=home&sid=aK1zAj5FZ9Io.

[13] Robin Sidel, Dennis K. Berman, and Kate Kelly, *J.P. Morgan Buys Bear in Fire Sale*, Wall Street Journal (Mar. 17, 2008).

[14] David Cho and Heather Landy, U.S. Government Assisting in Sale of Lehman Brothers, Washington Post online (Sept. 11, 2008) *available at* http://www.washingtonpost.com/wp-dyn/content/article/2008/09/11/AR2008091102580.html?referrer=email.

[15] Rick Brooks and Ruth Simon, *Subprime Debacle Traps Even Very Credit-Worthy As Housing Boomed, Industry Pushed Loans To a Broader Market*, Wall Street Journal at A1 (Dec. 3, 2007).

[16] Letter from Coalition for Fair & Affordable Lending to Ben S. Bernanke, Sheila C. Bair, John C. Dugan, John M. Reich, JoAnn Johnson, and Neil Milner (Jan. 25, 2007) at 3.

[17] *See, e.g.*, Glenn R. Simpson and James R. Hagerty, *Countrywide Loss Focuses Attention on Underwriting*, Wall Street Journal (Apr. 30, 2008).

[18] John Meacham and Daniel Gross, *The Oracle Reveals All*, Newsweek 32, 33 (Sept. 24, 2007).

[19] Vikas Bajaj and Christine Haughney, *Tremors at the Door – More People with Weak Credit Are Defaulting on Mortgages*, N.Y. Times at C1, C4 (Jan. 26, 2007).

[20] *Subprime Loans Defaulting Even Before Resets*, CNNMoney.com (Feb. 20, 2008). *See also* Atif Mian and Amir Sufi, *The Consequences of Mortgage Credit Expansion: Evidence from the 2007 Mortgage Default Crisis*, NBER Working Paper 13936, http://www.nber.org/papers/w13936; Benjamin Keys, Tanmoy Mukherjee, Amit Seru and Vidrant Vig, *Securitization and Screening: Evidence From Subprime Mortgage Backed Securities*, working paper (Jan. 2008).

[21] 73 Fed. Reg. at 14041.

[22] *Id.*

[23] Statement of Policy 2001-1, 66 Fed. Reg. 53052, 53055 (Oct. 18, 2001) (Department affirms the 1999 Statement of Policy that "simply delivering a loan with a higher interest rate is not a compensable service.").

[24] The link is explained in greater detail in our comments to the Federal Reserve Board's recent proposed Regulation Z rules under HOEPA. Comments of the Center for Responsible Lending on Proposed Rules Regarding Unfair, Deceptive, Abusive Lending and Servicing Practices pursuant to the Home Ownership and Equity Protection Act (Docket No. R-1305) (April 8, 2008) (hereafter "CRL HOEPA Comment").

[25] Fully two-thirds (66.6%) of the subprime MBS market share for 2007 included prepayment penalties, down only slightly from 69.1% in 2006. Inside B&C Lending, p. 3 (Feb. 15, 2008). Even as overall subprime originations plummeted since August 2007, 47% of asset-backed securities issuances of 4Q07 included payment penalties. Inside B&C Lending, p. 3 (Feb. 15, 2008); Inside B&C Lending, p. 2 (Jan. 18, 2008).

[26] A Study of Closing Costs for FHA Mortgages, Prepared for U.S. Department of Housing and Urban Development, Office of Policy Development and Research, Prepared by Susan E. Woodward, Urban Institute at x (May 2008). In her report, Dr. Woodward cites one study which concludes that brokered loans were not more costly than retail loans. *Id.* at 15. However, the study does so based on a database of subprime loans made from 1995 to 2002, contributed by ten subprime lenders, *see* Amany El Anshasy, Gregory Elliehausen, and Yoshiaki Shimazaki, *Mortgage Brokers and the Subprime Mortgage Market,* at 7 (May 2004). The contributors are not identified, other than by membership in a particular trade association, and we are concerned that the data from a self-selected and limited group of originators may create some selection bias, making it an unsuitable database, or at least one which must be treated with great caution. We note that three major originators with dominant market shares over that six-year period (and who were members of that trade association during some or all of that period) were the subject of law enforcement actions, Household, Associates and Ameriquest. *These actions resulted collectively in over $1 billion in penalties and restitution.* Additionally, at least two other major lenders during the early years of that period utilized a similar business model to two of the law enforcement targets but collapsed in bankruptcy. If this study is to be considered in any regulatory decision, we urge that, at a minimum, HUD consult with regulators familiar with the business models and practices in which these lenders engaged during the period, to determine whether the illegal practices might have affected outcomes reflected in loans in that database, making the data unreliable for some purposes.

[27] Howell E. Jackson and Laurie Burlingame, *Kickbacks or Compensation: The Case of Yield-spread premiums*, 12 Stan. J.L. Bus. & Fin. 289, 332 (2007); *see also* Patricia A. McCoy, *Rethinking Disclosure in a World of Risk-Based Pricing*, 44 Harvard J. on Legis. 123, 139 n.94 (2007) and sources cited therein.

[28] *Steered Wrong, supra* note 2.

[29] *Id.* That extra money, of course, is paid by the consumers in those subprime loans who could have—*should* have—been in the lower cost prime loans, and, but for the perverse incentives making those loans better for the middlemen, might have been.

[30] James K. Lacko & Janis K. Pappalardo, *Improving Consumer Mortgage Disclosures* at 74-76(Federal Trade Commission, Bureau of Economics Staff Report, June 2007). *See also* Ren S. Essene and William Apgar, "Understanding Mortgage Market Behavior: Creating Good Mortgage Options for All Americans," Joint Center for Housing Studies. Harvard University (2007).

[31] 12 U.S.C. 2607(a), (c)(2).

[32] Our comments to the FRB on its proposed HOEPA UDAP rules had offered specific definitions of subprime or higher-cost loans and "non-traditional loans" which HUD might adopt, or it might adopt the definition of "higher-cost loan" from the recently promulgated Fed HOEPA UDAP rules. *See* Comments of the Center for Responsible Lending on Proposed Rules Regarding Unfair, Deceptive, Abusive Lending and Servicing Practices pursuant to the Home Ownership and Equity Protection Act (Docket No. R-1305) (April 8, 2008); Federal Reserve System, 12 CFR Part 226, Truth in Lending; Final Rule (July 30, 2008), 73 Fed. Reg. 44522, 44533.

[33] Commonwealth of Massachusetts Attorney General's Regulations, 940 MA ADC 8.06(17), Mortgage Brokers and Mortgage Lenders – Prohibited Practices.

[34] This regulation precludes brokers from accepting compensation where there is a conflict of interest—functionally a ban on YSPs as the regulations define that conflict. Shortly after implementation, Wells Fargo changed its broker compensation system from "a sliding fee based on loan's profitability to a flat 1.5% of the loan amount." Binyamin Appelbaum, *Most Lenders Accept Tough New Mortgage Rules in Mass*, Boston Globe, (Jan. 10, 2008). The Massachusetts rule appears to be working to eliminate the perverse market incentives that have grown up around this practice.

[35] 73 Fed. Reg. 44565.

[36] 73 Fed. 14037.

[37] 73 Fed. Reg. at 14043.

[38] *See, generally*, *Steered Wrong, supra* note 2.

[39] Indeed, that practice is sadly common in the auto sales world, where a buyer loses the value of a down payment or a trade-in "credit" by the seller's simple act of raising the price of the car and add-ons to "swallow the down" or "swallow the trade." As with mortgage transactions, the more pieces at play in the pricing game, the harder it is for the consumer to keep track of them all.

[40] Predatory loan recipients often report that upon asking questions about a document that they didn't understand, they were told that it was just "red tape that the government requires" and that they "shouldn't worry about it."

[41] Some predatory lenders—retail as well as brokers—made a practice of strategically scheduling closings shortly before closing time, or at times or places otherwise designed to discourage questions or a careful review of documents.

[42] National Consumer Law Center, Comments on RESPA, Proposed Rule to Simplify and Improve the Process of Obtaining Mortgages to Reduce Settlement Costs to Consumers, Department of Housing and Urban Development, 24 CFR Parts 203 and 3500, Docket Number FR-5180-P-01 (June 2008) at 42-43.

[43] Written Statement of Ivy Jackson, Director, Office of RESPA and Interstate Land Sales, U.S. Department of Housing and Urban Development, Hearing before the Committee on Small Business, May 22, 2008.

AMERICAN
LAND TITLE
ASSOCIATION

Testimony of the American Land Title Association Before the House Financial Services Subcommittee on Oversight and Investigations

Presented by Gary Kermott
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Thank you for the opportunity to submit testimony on the proposed rule to amend the existing regulations of the Real Estate Settlement Procedures Act ("RESPA"). We respectfully submit this statement on behalf of the American Land Title Association ("ALTA" or "Association"), the national trade association of the land title industry. Our membership is composed of nearly 3,000 title insurance companies, title insurance agents, independent abstractors, escrow officers and attorneys who search, examine, and insure land titles to protect owners and mortgage lenders against losses from defects in title. Many of these companies also provide additional real estate information services, such as tax search, flood certification, tax filing, and credit reporting services. These firms and individuals employ nearly 100,000 persons and operate in every county in the country.

ALTA and its members commend the U.S. Department of Housing and Urban Development ("HUD" or "Department") for its stated objectives in the proposed rule. The Association agrees that it is important for consumers to better understand their real estate mortgage transactions, and to receive easy-to-understand and reliable information about loan terms and settlement costs to facilitate consumer shopping for mortgages and title-related services. We recognize that the Department has devoted substantial time to surveying the varying interests of settlement service providers and studying consumer reactions to proposed disclosures, and the Association applauds HUD's commitment to reforming its RESPA regulations.

We are concerned, however, that certain provisions of the Department's proposals will not achieve those objectives and, indeed, may create problems that undermine those objectives. For example: (1) the proposed Good Faith Estimate ("GFE") is long and complicated and does not allow for an easy comparison to the HUD-1 Settlement Statement ("HUD-1"); (2) the imposition of tolerances and volume discounts create an anti-competitive environment that could disadvantage small businesses and give consumers fewer choices of settlement service providers and; (3) the imposition of responsibility on the closing agent to read and interpret the closing script on behalf of the borrowers will increase costs for both sellers and borrowers.

We believe that RESPA reform cannot be resolved in one sweeping change without considering and appreciating the many moving parts of a residential real estate transaction. The Association, therefore, urges the Department to carefully consider the potential problems and impractical effects of the proposed rule, many of which we will discuss below. ALTA is committed to working with the Department to craft a solution that both benefits consumers and does not adversely affect the Association's members.

The Association's comments on the proposed rule are organized as follows: Part I provides an executive summary of this comment letter. Part II discusses several of the main concerns ALTA has with the proposed rule. This part focuses on

the Department's proposals for: (1) a closing script; (2) the disclosure of certain title insurance items on the GFE and the HUD-1; (3) the use of average cost pricing and related restrictions on government recording fees; and (4) negotiated volume discounts. Part III provides comments on other aspects of the proposed rule and responds to questions posed by the Department. Finally, Part IV concludes with alternative approaches to HUD's planned disclosures that ALTA believes will achieve the Department's objectives for the rule without the adverse consequences identified in Part II.

I. EXECUTIVE SUMMARY

Although ALTA supports the Department's underlying objectives for the proposed rule, the Association believes the Department is attempting, by regulation, to convert a statute and regulatory regime designed to (a) alert consumers to the range of closing costs they are likely to encounter (the GFE) and (b) provide a nationwide form that will reflect the distribution of the buyer's and seller's funds at closing (the HUD-1) into a new regime that was not intended by Congress and is not authorized by the statute. Irrespective of whether HUD's objectives are praiseworthy (and they are), the rule's new processes and procedures, which HUD deems necessary to achieve its objectives, are more than the statutory framework can bear.

A. <u>Closing Script</u>

We believe that HUD has absolutely no statutory authority to place on title companies and closing agents the obligations contained in its closing script regulations. Suggesting that HUD has such authority by characterizing the closing script as a mere "addendum" to the HUD-1 settlement statement only demonstrates that HUD itself cannot find the statutory authority for such obligations. We, therefore, believe that HUD is forced to find a tenuous link to some statutory provision for these very new, and very substantive, obligations.

Not only is there no statutory authority for HUD to impose these new regulatory requirements on title and closing agents, but, as a matter of sound policy, such new regulatory obligations can and should **only** be placed on the shoulders of the mortgage lender. There are a number of reasons why this is so.

First and foremost, under the proposed regulations, it is unclear what, if anything, the buyer/borrower or the closing agent can do if there are significant discrepancies between the final documents/ instructions sent by the lender at the time of closing and the terms of the loan or estimated settlement costs provided by the lender to the consumer at the application stage. The information HUD believes should be provided in the closing script is information that lenders should be required to provide at an earlier date – well before closing – so that the consumer

can take action on the basis of the new information before their rate lock expires or their moving van is packed. In short, the "education" that HUD wants to provide to consumers through the closing script comes too late in the process and from the wrong party to provide any benefit to consumers. It will only provide confusion.

Second, in many states, settlement agents risk engaging in the unauthorized practice of law by reviewing loan documents and answering borrower questions about final loan terms. The closing script, which postpones the resolution of any unclear terms until closing, will certainly place settlement agents in the position of either answering those questions, in violation of state law, or delaying the closing until the borrower can resolve those questions or concerns with their lender.

Third, in states where no such concerns over the unauthorized practice of law exist, the proposed closing script, contrary to HUD's estimate, will significantly increase the amount of time required for closing. In its estimate, HUD took into consideration only the amount of time necessary to read the script to the borrower. It did not include the significant amount of time that will be necessary to address questions or resolve discrepancies in connection with loan terms and final settlement costs. This will not only increase the amount of time required to close a transaction but, as a result, will decrease the number of closings a settlement agent can perform. These are factors that will almost certainly result in higher closing fees charged to the borrower and seller.

Finally, the Association believes that HUD may not fully appreciate the impracticalities that will prevent implementation of the closing script as proposed. For instance, not all real estate settlements are conducted face-to-face with the borrower, which makes it impossible to read aloud the closing script in such "escrow closings". Moreover, in the absence of a binding obligation on lenders to provide the closing script information to the closing agent well in advance of closing, the closing agent will be unable to prepare the closing script if there is any delay by the lender. ALTA, therefore, believes these insuperable problems suggest the mortgage lender is in the best position to prepare the closing script or an alternative document, which should be presented at some point prior to closing. This will ensure there is a meeting of the minds between the lender and the borrower as to what the lender thinks it is providing and what the borrower thinks he or she is getting. Requiring the closing agent to develop this mutual understanding at settlement imposes the obligation on the wrong party at the wrong time in the transaction.

B. Title Insurance Fee Disclosures

With regard to the GFE and HUD-1, ALTA asks the Department to reconsider the disclosure of certain title insurance services and fees on both of these disclosures. Most importantly, HUD should continue to require the itemization of all title-related charges on both the GFE and HUD-1, so that consumers can match

specific services to their individual needs and more easily shop for the title insurance services they desire. For example, lenders are primarily concerned with verifying that there are no liens against a property or judgments against their borrowerand may, therefore, be willing to accept a low cost, limited title search. Borrowers purchasing a property, on the other hand, want to know that they have good title to the land they are acquiring without easements and restrictions. These "clouds" on title can only be found through a more extensive and costly search. Unless the cost of a title search is itemized on the GFE and HUD-1, there will be no way for borrowers to compare the scope of the services that are included in the costs they are quoted.

In addition, we believe that use of the word "optional" to identify owner's title insurance is misleading to consumers and could conflict with state-specific practices that require owner's coverage in residential real estate transactions. The proposed disclosure of the title agent's and title underwriter's portion of the title premium also serves no useful purpose on the HUD-1 and does not aid consumers in their understanding of title insurance fees.

C. Recording Fees and Average Cost Price

While ALTA continues to question the Department's authority to impose tolerance limitations on estimates provided by lenders, we ask HUD to remove government recording fees from the proposed zero tolerance category. Such fees are rarely known to mortgage lenders or title insurance companies at the GFE stage, and there are a number of reasons why these fees may change before or after closing. Alternatively, if all settlement service providers were authorized to charge consumers the average cost price, the Association believes the certainty of the average cost price would benefit both consumers and our members, particularly as it relates to recording fees. Accordingly, if the Department's intent with the rule is to provide such authorization, we ask HUD to clarify these average cost price provisions.

D. Volume Discounts

Finally, it is the Association's position that volume discounts are anti-competitive and will disproportionately harm small businesses. Small independent title agencies do not have the resources to guarantee a stream of business to local title-related service providers or discount their own prices to compete with large national title providers. While such discounts may result in lower prices for the consumer in the short term, once the small businesses have been pushed out of the competitive marketplace, large providers are left to compete only among themselves. Under these circumstances, consumers will have fewer choices for title and closing related services, and prices will inevitably increase. Because this conflicts with HUD's stated objectives for the new regulations, we ask the

Department to reconsider the effects of volume discounts on both consumers and ALTA's members.

In addition, the use of volume discounts is inconsistent with state regulators' interest in protecting the solvency of title insurance companies. Because title insurance claims may come decades after purchase of the policy, state regulators have a strong interest in preserving the solvency of title companies to ensure that consumers are protected. State laws require that title premiums be "adequate." Severe discounting of title services could threaten the adequacy of the premium reserves.

E. Recommendations

Based on these concerns, ALTA proposes that HUD limit their efforts to simplifying the GFE and HUD-1 so that easy comparisons can be made. Page one of HUD's proposed GFE provides information about the loan terms and the total costs for settlement services in an understandable format. ALTA supports this type of summary page, but, in addition, ALTA urges HUD to improve individual fee disclosures by using a page that is identical to page two of the presentHUD-1. This would allow consumers to know what is included within the total amount listed on the GFE summary page and more directly compare the fees to the final charges at closing.

II. ALTA HAS SIGNIFICANT CONCERNS ABOUT HUD'S PROPOSALS

There are a number of important issues and problems raised by the proposed rule; however, for purposes of this correspondence, we focus on four particular aspects of HUD's proposals. The Association believes these four items could hinder a consumer's understanding of title insurance and settlement fees, increase ultimate costs to consumers, and have a severe adverse impact on our member's delivery of settlement services. We discuss each of these four items below.

A. The Responsibility for Ensuring that Consumers Understand Final Loan Terms and Settlement Costs Should Rest with the Mortgage Lender.

Following the Department's 2005 RESPA roundtables, settlement service providers expected HUD's eventual new and improved RESPA disclosures to focus on the GFE, which garnered the most attention in these discussion groups. While the Department has proposed drastic changes to the GFE in this proposed rule, HUD also has invented a new "addendum" to the HUD-1 in the form of a closing script. The closing script, however, is not a disclosure about which the Department sought input from settlement service industries, and, as a result, ALTA believes the

proposed disclosure is a flawed and impractical solution to "ensure that at settlement, borrowers are aware of final loan terms and settlement costs."[1]

A closing agent also fills a specialized role in a real estate settlement. The proposed HUD-1 addendum would impose new responsibilities and liabilities on the closing agent that most closers are prohibited from undertaking and which are not authorized or contemplated in any statutory provision of RESPA. In fact, this proposal would shift the closer from the position of an independent third party intermediary to an apparent agent of the lender. This is a significant and dangerous change to the essential role that title and other closing agents have traditionally played in the real estate process. Although the Association agrees that it is important for consumers to understand their mortgage loan and settlement costs, this is a responsibility best fulfilled by the mortgage lender who originates the loan and discloses settlement costs on the GFE.

1. Nothing in RESPA's Statute Authorizes HUD to Require a Settlement Agent to Prepare a Closing Script.

Initially, ALTA questions whether HUD has the statutory authority under RESPA to require settlement agents to prepare and provide a closing script. This is a brand new concept, which we assume HUD derives from its statutory authority to develop a uniform settlement statement. However, nothing in these statutory provisions remotely authorizes the kind of new and substantive obligations that HUD is seeking to impose on title and closing agents. The Department cannot hide this lack of authority by claiming these obligations are merely an "addendum" to the HUD-1 form. Instead, if HUD were to use any statutory authority for imposing such obligations on anyone, that authority can only be derived from the obligations RESPA imposes on **lenders** to provide the GFE.

2. To Comply With HUD's Proposed Closing Script, Closing Agents Risk Committing the Unauthorized Practice of Law.

According to the proposed regulations, HUD proposes to require the "settlement agent or other person conducting the settlement" to read the closing script aloud to the borrower and explain, among other things, the loan terms as contained in the mortgage documents. By placing a closing agent in the role of explaining loan terms and settlement charges, a consumer is likely to view the closing agent as an expert who can advise the consumer as to the particulars of the transaction or answer any question regarding their loan. However, many states allow only licensed attorneys to answer borrower questions and explain the details of a mortgage loan transaction. If HUD requires a settlement agent to be responsible

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[1] 73 Fed. Reg. 14030, 14033 (Mar. 14, 2008).

for reviewing loan documents and explaining the loan terms to a borrower at closing, the agent may be forced to commit the unauthorized practice of lawunder many state laws. Alternatively, only attorneys will be able to close transactions in those states, which will undoubtedly increase settlement costs.

For example, in Virginia, title insurance companies and agents must adhere to the state's Unauthorized Practice of Law Guidelines for Real Estate Settlement Agents ("Guidelines").[2] While a title entity may conduct the closing, prepare the HUD-1, receive and disburse funds, and record mortgage documents, the entity is prohibited under the Guidelines from drafting legal instruments and explaining the legal obligations of the parties under the loan documents. Similarly, the North Carolina State Bar has identified a list of services, which if performed by a non-lawyer, will constitute the unauthorized practice of law in the state. One such service is:

> Provid[ing] a legal opinion or advice in response to inquiries by any of the parties [at closing] regarding legal rights or obligations of any person, firm, or corporation, including but not limited to the rights and obligations created by a promissory note, the effect of a pre-payment penalty, the rights of parties under a right of rescission, and the rights of a lender under a deed of trust.[3]

Accordingly, if a title company or other non-lawyer closing agent in states like Virginia or North Carolina is required to read aloud a closing script to the borrower, the closing agent would be prohibited in those states from providing any explanations to the borrower with regard to the loan terms identified in the closing script. If HUD's objective for the closing script is to ensure that consumers understand their mortgage loan, a closing agent precluded from providing explanations to the borrower is the wrong person to provide this clarity. Instead, if certain loan term information is to be emphasized to the borrower at or prior to closing, the mortgage lender originating the loan should be tasked with this explanation.

3. The Proposed Closing Script Will Increase the Time Required for Closing and Resulting Closing Fees.

The Department spends a considerable amount of time in the proposed rule and in its Regulatory Flexibility Analysis discussing the amount of savings consumers will enjoy as a result of HUD's proposed disclosures in the rule. Yet, with

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[2] See "Unauthorized Practice of Law (UPL) Guidelines for Real Estate Settlement Agents," Parts V and VI, available at www.vsb.org/site/regulation/upl-guidelines-for-real-estate-settlement-agents.

[3] Authorized Practice Advisory Opinion 2002-1, N.C. State Bar, Jan. 24, 2003.

regard to the proposed closing script, the rule fails to appreciate the amount of additional time it will take a closing agent to prepare and read the closing script, and the effect this will have on a closing agent's resulting fee. In fact, HUD estimates that it will take an additional 45 minutes to close a loan with the closing script. This, however, is an underestimation if the goal of the script is to ensure borrower questions are answered and consumers leave the closing table understanding the terms and the costs of their loan. Our members estimate an additional 30 minutes will be needed just to respond to the questions raised by the closing script.

More specifically, HUD does not appear to anticipate the fact that borrowers will ask questions about the items identified in the closing script that the settlement agent may be unable to answer due to the legal prohibitions discussed above or a lack of knowledge and information. If state unauthorized practice of law provisions prohibit a closing agent from explaining loan terms to a borrower and a borrower has questions, a closing agent will be forced to stop the closing and contact the lender for the proper answers and explanations for the borrower. Similarly, the borrower may ask why there is a discrepancy between the final and estimated settlement charges the lender provided. The timeliness of these answers is dependent on the lender and whether the appropriate person can be reached in a single telephone call during the lender's normal business hours.

As a result, a normal hour-long closing may turn into two or even three hours to answer the borrower's questions, and the settlement agent will be forced to scale back the number of closings the agent can complete in one day. That will substantially increase the burden on closers, especially small independent businesses. With fewer daily closings, the settlement agent may be forced to increase its closing fees to sustain its operations. Although HUD already anticipates a $54 increase in closing fees to account for the time spent reading the closing script, the Association is concerned that this is too low by an order of magnitude.

The proposed rule also fails to recognize that most closings occur at the end of the month. There are many reasons for this, including the payment of daily taxes and interest charges, to name a few. HUD's economic analysis, however, fails to take into account that closers will not have the physical space or the man power to accommodate the same number of closings at the end of the month given the increased time necessary for completion of the closing documents and explanations. This will disproportionately harm smaller settlement companies and agents.

If HUD's response to these points is that the closing agent need not answer any questions that the consumer may have, then the closing script obligation will either result in a very unhappy consumer– one whose anger will be more directed at the closing agent than the lender– or the closing script could just as easily have been delivered in writing by the lender to the borrower after closing. In other words, if HUD is not expecting a consumer to be able to take any action at the closing table

as a result of having heard the closing script, then why is it essential that the closing script be provided to the borrower at the time of settlement?

Given these issues, ALTA believes the Department can eliminate any uncertainty regarding the time required to close a transaction by shifting the responsibility to explain loan terms and final settlement charges to the lender. The lender is responsible for the ultimate loan product reflected in the mortgage documents to be signed at the closing table. If the Department is concerned about resolving situations where a borrower is unaware or unsure of the terms of the loan, it should be the lender's responsibility to identify exact loan terms and explain them to the borrower before he or she gets to the closing table. Otherwise, the closing agent merely identifies final loan terms for the borrower without any ability to ensure the borrower understands them. This process could prove to take more time and be more expensive, with less benefit to the consumer, which is contrary to the Department's stated objectives for the rule.

4. The Proposed Rule Provides No Guidance for Settlement Agents When Inconsistencies in Mortgage and Closing Documents are Identified.

In preparing the closing script, the proposed rule obligates the settlement agent to disclose and explain to the borrower any inconsistencies between the mortgage note, between related settlement information and the GFE, and between the HUD-1 and the GFE. Other than this instruction, the rule fails to provide any guidance for the settlement agent to take action when these inconsistencies are identified. For instance, the rule provides no guidance for the settlement agent in circumstances where the lender exceeds the applicable tolerances or has changed the terms of the loan from that expected by the borrower. The rule is clear, however, that exceeding the tolerances violates Section 4 of RESPA. But, what is the settlement agent to do? If the lender exceeds the stated tolerances by $96 (as set forth in Example 6 of the sample closing scripts)[4] and the settlement agent closes the transaction, the settlement agent may find itself the defendant in a class action lawsuit.

In addition, HUD states that its intent for the closing script is to ensure borrowers are aware of and understand the loan terms. The rule, however, does not address how a settlement agent should proceed with the closing when the final loan terms are not the same as the loan terms disclosed on the GFE. If the settlement agent is prohibited by state law from explaining loan terms to the borrower and the lender is unreachable at the time of settlement, the closing agent may be forced to

[4] See 73 Fed. Reg. at 14089-14092.

delay the closing. This is small comfort to a consumer whose worldly possessions are in a moving van parked outside the settlement agent's office.

Furthermore, the rule subjects certain settlement charges to different tolerances depending on whether the borrower uses a lender-recommended settlement service provider or shops independently for a provider. In completing the comparison chart portion of the closing script, the rule does not identify how a settlement agent is supposed to know which service providers are borrower-selected and not subject to tolerance calculations. This is yet another example of how HUD's proposed rule puts the settlement agent on the spot to resolve issues created by the lender, which, without instructions from the lender, cannot be resolved. ALTA believes the proposed closing script rules fall short of providing realistic instructions to make the disclosure useful to the consumer.

5. Implementation of the Proposed Closing Script Creates Several Practical Problems.

The Department's proposed rule also fails to appreciate the realities of modern-day real estate settlements. As a result, the Association is concerned that the rule, if finalized, would be impractical and impossible to implement.

For example, the proposed rule would require the settlement agent to read the closing script aloud to the borrower at closing. Such a requirement assumes that all residential real estate closings are conducted face-to-face with the buyer and the seller around an actual closing table. However, not all residential real estate closings are conducted in this manner. On the West Coast, escrow companies conduct closings and arrange for the transfer of real estate without the buyer and seller having to be present at a face-to-face closing. In addition, more and more settlement companies offer the convenience of closings by mail or via the internet, where buyers and sellers separately receive final closing and mortgage documents, execute them in the presence of a self-selected notary, and return them to the settlement agent by the scheduled closing date. In each of these circumstances, escrow officers and/or settlement agents do not meet with the borrower faceto-face and would not have the opportunity to read a closing script to the borrower. Yet, the proposed rule provides no alternatives and would not allow a settlement agent to forego the reading aloud component of the closing script. Given the varying procedures for real estate closings across the country, this requirement is impractical and impossible to implement as designed by the Department.

Moreover, HUD's proposed rule is silent with regard to the language of the closing script, although the examples provided in the rule show the closing script only in English. Borrowers, however, often speak languages other than English, and the rule does not address whether the Department expects the settlement agent to translate the script into the borrower's language. If a settlement agent must read

aloud a script in a face-to-face closing and obtain the borrower's written acknowledgment that the settlement agent explained the loan terms, this may be an impossible task if the borrower does not speak and understand English. HUD states that its purpose for the closing script is to ensure that borrowers are aware of the final loan terms and settlement charges; yet the Department fails to appreciate that language could be the first barrier to a borrower's understanding of these items.

Finally, the rule fails to appreciate the time frame within which a settlement agent must prepare for closing. Although the rule would require the loan originator to transmit to the settlement agent the necessary information to complete the closing script, the rule fails to obligate the loan originator to provide such information within a specified period of time to ensure the settlement agent is able to prepare the closing script and provide it to the borrower 24 hours prior to closing. In fact, settlement agents often do not receive the closing package and instructions from the lender until shortly before closing. Should a lender fail to provide a settlement agent with the required information in a timely fashion, the closing agent risks the additional liability that could result from its failure to prepare and provide the borrower with a copy of the HUD-1 and closing script prior to closing. Furthermore, at this point, the settlement agent has little time to prepare the actual closing script, which could threaten a settlement agent's ability to close the borrower's transaction in a timely fashion. Accordingly, not only is timing an impractical (or missing) aspect of the proposed closing script, it is yet another reason why mortgage lenders are best suited to explain final loan terms and settlement charges to their borrowers.

B. The Disclosure of Certain Settlement Services and Title Insurance Fees is Misleading and Could Discourage Consumer Shopping.

Although one of HUD's purposes for the proposed rule is to simplify and improve consumer disclosures, ALTA believes certain of the rule's disclosures related to settlement services and title insurance fees are misleading, could discourage consumers from shopping for services that are in the buyer's best interest, and could competitively disadvantage the Association's members. ALTA fully supports the Department's objective of clarity, but we believe the rule goes too far in simplifying the disclosure of settlement services and could create confusion about the role of title insurance in the settlement process.

1. The Disclosure of a Single Price for "Primary Title Services" Does Not Allow a Consumer to Comparison Shop.

In a departure from current requirements regarding the itemization of settlement charges in both the GFE and on the HUD-1, the proposed rule would require that a single fee be disclosed for "title services and lender's title insurance" in

block 4 of the GFE and for "primary title services" in the 1100 section of the HUD-1.[5] The elimination of required itemization for these fees is of immense concern to ALTA and can only serve to lessen, rather than enhance, competition for these services.

HUD's belief that (a) consumers shop among lenders based on the lender's estimates of the 1100 series charges, and (b) that consumers have no need to know the amounts of the various charges that comprise the aggregate amount is in error. In a purchase/sale transaction, the title-related and closing-related charges in the transaction are **not** a function of the lender's needs, but are far more a function of the needs of the buyer and seller of the property with regard to their underlying real estate transaction. In most cases, the seller (in seller-pay jurisdictions) and the buyer will have decided on the provider of title and closing services before the lender is even involved in the transaction. Thus, how the lender estimates the costs for these services should be unrelated to how buyers decide on the lender that offers the best loan at the best lender-related costs.

With regard to the itemization of individual costs that comprise the aggregate block 4 (or 1100 series) charge, consumers who want to shop for these services will be seriously disadvantaged because there is no way to determine the lender's estimated price for the title company, the escrow company, the attorney, or the surveyor. In fact, the concept that only the aggregate amount of title and closing-related charges need be disclosed is an unfortunate – and inappropriate – hangover from HUD's ill-fated "packaging" proposal in 2002. In that proposal, HUD believed – erroneously – that if a lender packages all settlement charges, the borrower has no interest in knowing what the individual charges in that package might be. Even if that view has validity in the case of a refinance loan, it has no validity in the case of a purchase/sale transaction or in the proposed regulations. HUD and ALTA ultimately want to encourage consumers to shop among providers of title and closing-related services. A lender who provides a GFE that only discloses an aggregate figure for a range of individual charges prohibits the consumer from shopping for the title (or escrow) services at a lower price than that reflected in an aggregate price on the GFE.

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[5] ALTA also is concerned that HUD has effectively altered its long-standing definition and guidance regarding core title services. Notably, the rule would define "primary title services" to include "any service involved in the provision of title insurance (lender or owner policy) and <u>settlement or closing services</u>, including but not limited to: title examination and evaluation; preparation and issuance of title commitment; clearance of underwriting objections; preparation and issuance of a title insurance policy or policies; and the processing and administrative services required to perform these functions." 73 Fed. Reg. at 14056 (emphasis added). This is a sharp contrast to HUD's current definition of core title services, which includes the conducting of a closing only <u>where customary</u> and when the agent's compensation for such services is customarily <u>part of the payment or retention from the insurer</u>. 24 C.F.R. § 3500.14(g)(4); 61 Fed. Reg. 49,398-49,400 (emphasis added). If the Department's concept of core title services is changing with the proposed rule, this is an issue ALTA urges HUD to directly address in any final rule.

Similarly, with regard to the HUD-1, the entire purpose of the document is to provide a record for all parties as to how the settlement funds brought to the transaction by the buyer, seller and lender are disbursed. This information has been of value in numerous studies to determine the average or typical charges for various settlement services. But HUD's proposed handling of the 1100 series charges would undermine those objectives. By lumping together so many different charges into the category of "primary title services," no one who reads the HUD-1, including the buyer and the seller, will know how their funds were actually disbursed and to what providers.

Moreover, what exactly constitutes "primary title services" is not clear. HUD's explanatory statement describes a "primary title service" as including abstract, binder, copying, document handling, or notary fees, even if a party other than the title company listed on line 1101 provides the service.[6] However, the definition of "primary title service" in the proposed regulation is different from that description. The proposed regulation defines "primary title service" as "any service involved in the provision of title insurance (lender or owner policy) and settlement or closing services, including, but not limited to, title examination and evaluation, preparation and issuance of title commitment; clearance of underwriting objections; preparation and issuance of a title insurance policy or policies, and the processing and administrative services required to perform these functions."[7] What about title searching, abstracting, "binder," copying, document handling, document preparation, notary fees, handling of the closing, and escrow services? These services seem to be dropped from the official definition.

The instructions for completing the HUD-1[8] also indicate that those charges not encompassed by "primary title charges" include "closing attorney or escrow agent" charges. Does this mean that the closing charges made by an independent escrow company should be listed separately from "primary title services," whereas the charge for a closing made by a title company is part of "primary title services"? Similarly, while "attorney closing" services are not "primary title services" and are to be listed separately, what if the attorney is not providing closing services, but some other service, such as the examination of title? Should the attorney's fee for this "primary title service" be included in the aggregate charge? These are the types of questions that support the continued itemization of title-related services.

Finally, the disclosure of a single fee for title insurance also fails to recognize that, in most areas of the country, the seller generally pays a substantial portion of

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[6] 73 Fed. Reg. at 14049.

[7] Id. at 14056.

[8] Id. at 14060.

the title insurance charges. The Department appears to assume that the borrower pays for all closing costs, including the fees for "primary title services," and the proposed rule provides no instruction as to how to disclose title-related fees when these costs are paid by the seller. If the GFE and HUD-1 do not itemize the fees for title insurance services, the Association believes it is possible the borrower could pay for services sellers currently assume, which will only result in higher costs to the borrower. Without evidence that consumers do not currently understand the title insurance-related fees disclosed in the current 1100 series of the HUD-1, ALTA asks the Department to continue to require such fees to be separately itemized on both the GFE and HUD-1.

2. The Word "Optional" Should Be Removed From the Disclosure of Owner's Title Insurance.

On both the proposed GFE and HUD-1, the Department would require the cost for owner's title insurance to be disclosed separately as "Optional owner's title insurance." This reflects HUD's continuously mistaken view that, in real estate transactions, it is the loan policy that is the key policy and the owner's policy is a mere addition to the loan policy. In a purchase/sale transaction, exactly the opposite is generally the case. It is the owner's policy that is the major policy in the transaction, and the loan policy is an "add on" that is issued at a relatively small additional premium.

Moreover, by including the term "optional" in both disclosures, HUD appears to be suggesting that a consumer does not need separate coverage for title insurance, which may discourage borrowers from obtaining owner's coverage. The Association understands that it is HUD's intent to create better disclosures to reduce the consumer's overall settlement costs, but by isolating owner's title insurance coverage as a service that can be eliminated to lower fees, the Department is targeting the one item that is structured to protect the consumer in connection with a real estate transaction. The purchase of a home is the most expensive purchase most consumers will ever make, and RESPA disclosures should not in any way discourage consumers from protecting their investment.

The use of the word "optional" also ignores several significant realities regarding the sale of title insurance. Notably, in many states, owner's coverage is required in residential real estate transactions. For example, although real estate and insurance laws in Washington State do not require anyone to obtain title insurance, real estate is transferred in the state by "warranty deed," which requires the seller to guarantee to the buyer that the seller actually holds the ownership rights being sold. As a result, sellers are required to purchase title insurance protecting the buyers in Washington, which is a standard clause in real estate listing

agreements.[9] By labeling owner's title insurance as optional on both the GFE and HUD-1, HUD's directive would directly conflict with requirements for the purchase of title insurance in Washington and other states. Should a consumer in one of these states elect not to purchase owner's coverage based on the GFE disclosure, consumers will only be confused when the title insurance company requires an owner's title insurance policy to close the transaction.

Even if an owner's policy is not required, many sellers often elect to purchase owner's title insurance policies for buyers. In those states where such is the custom, the rule provides no instructions as to how to disclose the cost of an owner's title policy on the GFE. Arguably, including the cost on the GFE would require the fee to be added to the consumer's total estimated settlement charges, which inflates the charges for which the consumer ultimately is responsible. On the other hand, if the cost is left blank on the GFE, the Department should expect the consumer to be confused when he or she sees the cost for owner's insurance disclosed on the HUD-1 (even if this cost appears in the seller's column of the disclosure).

HUD also fails to appreciate the fact that it is more cost effective for the consumer when a lender's policy and an owner's policy of title insurance are purchased concurrently.[10] A title search must be performed in connection with every issuance of a title insurance policy. When a title insurance underwriter can issue both a lender's policy and an owner's policy in connection with a single title search, the price of both policies costs less than if a consumer were to purchase his own title insurance policy after closing. Further, the purchase of an owner's policy at closing frequently results in savings to consumers in the future through the application of readily-available discounted "reissue" rates when borrowers refinance their loans or sell their properties. These are savings that consumers should not be discouraged from taking advantage of, particularly at the GFE stage when consumers ideally are shopping for a mortgage loan. Thus, while ALTA has no objection to the disclosure of the cost of owner's title insurance separately from a lender's policy, including the word "optional" in the disclosure is misleading and could result in higher costs for consumers in the long run. It is the Association's position that HUD should remove "optional" from both the GFE and HUD-1.

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[9] See "Title Insurance in Washington: Improving Competition and Consumer Choice," Report of the Title Insurance Review Task Force (Sept. 2007), available at www.insurance.wa.gov/publications/news/2140-Report.pdf.

[10] The rule fails to appreciate that the price for title insurance could be vastly different depending on whether only a lender's policy is purchased or both lender's and owner's policies are purchased. The rule provides no instructions as to whether the price for title insurance should be disclosed with the assumption that a consumer may choose not to purchase the "optional" owners policy or on the assumption that both policies will be issued simultaneously.

3. Itemizing the Split in Title Insurance Premiums Serves No Useful Purpose on the HUD-1.

The proposed HUD-1 includes two disclosures that HUD does not propose for the GFE. In lines 1113 and 1114 of the new HUD-1, the closing agent would be required to disclose the title agent's portion and title underwriter's portion of the total title insurance premium. Although the preamble to the proposed rule is silent with regard to the Department's reasons for such a disclosure, HUD refers to its decision to exclude such a disclosure from the GFE in its Regulatory Flexibility Analysis. With an intent to eliminate items that would place a greater burden on small businesses, HUD states that it is:

> Dropping the Title Agent/Title Insurance Premium Breakout. Title agents argued that breaking out the title insurance premium that goes to the underwriter from the rest of the title charges is costly and serves no useful purpose. This requirement has been eliminated, so there will be no compliance burden associated with the title agent/title insurance premium breakout on the GFE. *The breakout was not useful for comparison shopping.*[11]

For all of the reasons that HUD identifies above, the Association questions whether such a premium breakout serves any useful purpose on the HUD-1. The compliance burden on small title agencies in making this disclosure is no different for the HUD-1, and the disclosure certainly does not aid a consumer in understanding the title insurance fees paid as part of final settlement charges. In fact, the premium disclosure has nothing to do with the final prices the borrower pays at the closing table.

Moreover, the closing agent, if it is not also the title insurance agent in the transaction, will not know a title agent's premium split and HUD has no authority to require that title insurance agents inform the person handling the closing (such as an escrow company in western states) of the agent's level of commission in the transaction. Furthermore, no other insurance agents (i.e., homeowners, auto, and life insurance) are required to disclose the percentages of insurance premium they receive as compensation. The same is the case for other settlement service providers, such as real estate agents, who are not required to disclose the percentage of the real estate commission retained by the real estate sales person and the portion retained by the real estate brokerage company. Absent a clear statutory basis and sound policy reason for requiring title insurance agents to be singled out and forced to disclose their commissions from the title insurance company, there is no basis for HUD to require this disclosure in the HUD-1.

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[11] 73 Fed. Reg. at 14109 (emphasis added).

C. All Settlement Service Providers Should Be Authorized to Charge Consumers the Average Cost of Settlement Services to Maximize the Benefit to Consumers.

ALTA applauds the Department's proposal to allow average cost pricing in an effort to protect consumers from high settlement costs. However, as written, the Association believes the rule does not go far enough to maximize potential cost savings to consumers. The proposed rule generally would allow the cost for a settlement service provided by a third party to be an average price, but the two methods proposed for calculating the average price are both based on practices of the loan originator. Accordingly, the rule appears to effectively allow only the loan originator to measure and charge the average cost price for settlement services performed by third parties. This excludes other settlement service providers, like the Association's title insurance and settlement company members, who could use average cost pricing as an important tool in providing competitive and guaranteed prices for title-related services. This is particularly significant as it relates to government recording fees, which the rule proposes to subject to a zero tolerance or, in other words, prohibit from increasing at the closing table.

Before considering the benefit of allowing title and settlement companies to calculate their own average cost price, it is imperative that ALTA comment on the Department's plan to subject government recording fees to a zero tolerance standard in a lender's GFE. In creating such a restriction, the Department ignores the reality that the amount of government recording fees chargeable to the consumer fluctuates throughout the origination process. HUD, instead, focuses on the fact that government recording fees are set by local regulations or ordinances and are well known to mortgage lenders at the time they receive a GFE application and provide a GFE disclosure to the consumer. While it may be true that lenders know that recording fees in a certain county are, for example, $2.00 for the first page and $1.25 for every page thereafter, it is impossible for a lender to know the exact number of pages that will be recorded following settlement.

Even if a standard Fannie Mae loan document in a state is 12 pages long (and would equal $15.75 in recording fees using the example above), there are many reasons why the number of pages to be recorded can change during the origination and title search process, which will always change the amount of recording fees. For instance, the addition of another signature page to the mortgage document or a need to include the property description on an exhibit page to the deed will increase the number of pages to be recorded as well as the resulting recording fees. In addition, if the title company discovers a lien on the property during a title search, a lien release must be recorded to perfect the chain of title. Each of these extra recordings will result in additional fees, which are circumstances that neither a mortgage lender nor a title company can anticipate at the time a consumer receives a GFE. As a result, it is unrealistic to expect mortgage lenders to

disclose exact recording fees on the GFE and impractical not to allow these fees to change at the closing table. The Association asks the Department to reconsider its proposal to subject government recording fees to a zero tolerance under the rule.[12]

Of equal importance, the new regulation on average cost pricing is contained in the provision (§ 3500.8(b)(2)) that governs the completion of the HUD-1. This is not where the clarification is needed. It makes no sense to include a provision on "averaging" in a HUD-1 section of the regulations when such a provision is needed to permit lenders and others to apply average cost pricing without running the risk of violating § 8(b) of RESPA. The proposed regulations fail to clarify that average cost pricing is not a violation of § 8(b). HUD should ensure that its regulations relevant to that section of RESPA are amended to reflect its new policy on average cost pricing.

Ultimately, ALTA believes that if the rule would allow title and settlement companies to use the average cost price, particularly as it relates to recording fees, express delivery charges and other third party charges for which title companies must pay, consumers would benefit from the certainty the average cost price provides. Moreover, the average cost price could curb the significant threat of class action litigation for title insurance and settlement companies as it relates to recording fees. Notably, class action plaintiffs' lawyers recently have filed lawsuits against title companies based on the allegation that an overcharge in recording fees is a violation of Section 8(b) of RESPA. Yet, these overcharges are not intentional and occur because last-minute changes to the mortgage documents result in a fluctuation in the recording fees. If a title or settlement company were able to determine their average cost for recording fees in particular geographic areas and pass this average through to the consumer, ALTA's members could refocus their resources currently spent on costly class action litigation. In the end, any potential for an overcharge in recording fees is made up by lower costs for other services disclosed on the GFE. The Association, therefore, believes that it is in everyone's best interest to authorize all settlement service providers to charge settlement fees based on average cost pricing without fear of violating HUD's interpretation of § 8(b) of RESPA. If the Department's intent with the rule is to provide such a broad authorization, we ask HUD to clarify the application of the provisions in the proposed rule.

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[12] The proposed rule also states that a lender must estimate the sum of all state and local government fees, charges, and taxes, but does not instruct whether the lender must disclose only the borrower's portion of these fees. In many cases, the seller is responsible for certain recording fees, and the rule does not address whether the "sum" must include the seller's recording fees. As a result, not only should the Department reconsider subjecting total recording fees to a zero tolerance standard, but the rule should revisit the instructions it provides for completion of the GFE to be sure borrowers are shown and ultimately charged for only those government recording fees for which the borrower is responsible.

D. The Allowance of Volume Discounts is Anti-Competitive and Will Disproportionately Harm Small Businesses.

1. Small Title Companies Cannot Compete With Discounts Offered by Large Title Companies.

HUD's proposal to allow settlement service providers to negotiate volume discounts will disadvantage small title insurance companies that do not have the resources to discount their services in the same way as large companies. Yet, based on the rule's lengthy Economic Analysis, the Department seems to assume that such a proposal will not have anti-competitive effects or disadvantage small title insurance businesses. This is not the case.

In discussing the rule's impact on small businesses, the Department focuses on the local nature of title and settlement services and highlights the perceived advantages of knowledge and networks of clients that HUD says should not be negatively impacted by the rule. In fact, HUD predicts that RESPA reform will provide opportunities for efficient third-party firms to expand their operations. HUD goes on to state that "there is not evidence to support arguments that these 'locally-provided' services will shift to larger businesses. . . . [L]arge national title companies have to rely on local title companies in order to serve all areas."[13] Based on these comments, ALTA believes the Department is misunderstanding the anti-competitive arguments the Association made in 2002 and continues to make in response to the current proposed RESPA rule.

Notably, HUD's comments are focused on certain title-related services, such as the title search and settlement, which are local services often conducted by businesses located in the same geographic location as the subject property. As a result, it is true that when title insurance is provided by a large national company, the title search and closing services are subcontracted to local companies. This, however, is unrelated to the purchase of title insurance generally, which consumers could elect to buy from small independent title insurance agencies or a large national title provider with an office in the same geographic location.[14] In either case, the title

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[13] "Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis," Ch. 3, pp. 3-139 n. 141, available at www.hud.gov/offices/hsg/sfh/res/200803/5180RIA.pdf [hereinafter Regulatory Impact Analysis].

[14] This is evident by the Department's focus on "Title Abstract and Settlement Offices" in its Regulatory Impact Analysis on small businesses. HUD states that "Title Abstract and Settlement Offices" are defined as companies that: (1) research public land records to gather information relating to real estate titles; (2) prepare documents necessary for the transfer of title, financing, and settlement; (3) conduct final real estate settlements and closings; and (4) file legal and other documents relating to the sale of real estate." The Department also notes that that the term "title agent" is frequently used in the Regulatory Impact Analysis to refer to "Title Abstract and Settlement Offices." See Regulatory Impact Analysis, Ch. 5, pp. 5-92 n. 136. HUD, however, fails to recognize

search is a service that both the small agency and the large provider must order before a title insurance policy can be issued. However, the rule and its proposals for negotiated volume discounts will create an uneven playing field where the large national lenders and large national title companies will be able to undercut small local firms on title search prices.

When a consumer is faced with the choice of a small independent agency and a large national provider in the same geographic location to purchase title insurance, the ability to negotiate volume discounts on the local services that are incidental to the issuance of a title policy (i.e., the title search) will disadvantage the small independent agency that does not have the resources to guarantee a stream of business to a third party or discount its own services when the services are performed in house. For example, if a large provider subcontracts the title search to another company, the large title company has the flexibility to pass through a discounted fee for the title search to the consumer.[15] Because the large provider's volume of business is higher nationwide, the large provider is better positioned to absorb the difference between the discounted prices passed through to the consumer and the actual fee paid to the title search company. The small independent agency, on the other hand, likely performs the title search services in house and depends on the income produced from its title search fees to sustain its operations and compensate its handful of employees. The small agency, therefore, is competitively disadvantaged as compared to the large provider when it cannot offer the same kinds of discounts to consumers.

Similarly, title insurance companies often are required, at the request of the lender or the borrower, to overnight packages of closing documents in preparation for the settlement or after the settlement has occurred. Because large national title providers have reason to use overnight delivery services more frequently than small providers, large title companies are able to negotiate discounted overnight delivery rates and pass these discounted rates through to the consumer. A small independent title agency, however, is not in a position to negotiate corporate delivery

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that the kinds of services that define "Title Abstract and Settlement Offices" are not the core title services performed by title agents. While title agents may conduct title searches, prepare documents, conduct the closing, and record documents, these are services that often are subcontracted to local service providers, which is the focus of the Department's discussion. Title insurance agents, which may be small or large companies, are defined by the core title services they perform, including the evaluation of the title search to determine insurability of the title, the clearance of underwriting objections, the issuance of a title commitment, and the actual issuance of the policy or policies on behalf of the title insurance company. Small title insurance agents that perform these core title services are the companies that will be competitively disadvantaged by the proposed rule.

[15] This example assumes that the cost for title insurance does not include the cost of the title search. In some states, the total price for title insurance includes the cost for the title search and other incidental services (i.e., all-inclusive title insurance rate).

rates and cannot compete with the lower prices the large provider can charge its consumers. Moreover, even if the small agency were to match or beat the prices charged by the large title company, the small agency is less able to absorb the costs it does not pass through to the consumer.

Under these circumstances, the ability to negotiate discounts and pass them through to the consumer disadvantages the small title insurance agency who is unable to compete with the lower prices offered by large title insurance providers. While this may result in lower prices for the consumer in the short term, once the small title companies have been pushed out of the competitive marketplace, large providers are left to compete only among themselves. Under these circumstances, the laws of economics teach us that prices eventually will increase and be higher for the consumer, which conflicts with the Department's stated objectives for the rule.

2. Mortgage Lenders Will Favor Large Title Providers Who Offer Discounts or Their Own Affiliate Providers.

In addition to the competitive disadvantages small title companies will experience as a result of negotiated discounts, ALTA is concerned that mortgage lenders and brokers will add to the anti-competitive effects by favoring affiliated title companies or those companies that can provide title related services on a nationwide basis. Lenders are most likely to select these companies in order to more easily manage their network of service providers and the costs they must estimate.

Notably, in connection with the Department's proposals for the new GFE form, the fees for third-party settlement services, when these services are obtained from providers recommended by the lender, are subject to a 10% tolerance. By contrast, if the borrower shops for and selects his own third-party service providers, the rule proposes no restriction on the amount the fees may increase at closing. While the Association understands that these differences in tolerances are designed to hold loan originators accountable for the prices quoted on the GFE, ALTA is concerned that such a system will result in lender-created teams of settlement service providers. The lender's message to the borrower then will be: "select other settlement service providers at your own risk; we cannot guarantee that the final prices charged by those self-selected providers will not increase at closing." By virtue of emphasizing these "guaranteed" prices to consumers, lenders are able to influence and encourage a borrower's selection of a recommended provider. Yet, there is no guarantee that these recommended service providers are the least expensive or the best. Moreover, this "preferred provider" concept would take the title agent out of the role of independent fiduciary to the *transaction* and place it in the role of "sub-contractor" to the lender.

The Association is fully aware that the circumstances described above may initially result in the consumer's receipt of lower costs for title insurance and other third-party settlement services. However, these initial savings come at the expense of small title insurance providers that are unable to offer the same substantial discounts and will not make the list of lender-recommended companies. The inability to offer substantial negotiated discounts alone is enough to harm the businesses of small providers; if these companies also do not get the recommendation of loan originators, small title insurance providers will be pushed out of the marketplace. As noted above, if a limited number of large title companies are able to dominate the market, the prices for their services eventually will increase, and the incentive to compete for a borrower's business will no longer exist. The Association, therefore, urges the Department to consider these unintended consequences of the proposed rule and pursue changes that will foster an even playing field. To create a truly competitive marketplace and ensure that borrowers shop for settlement services (not just a mortgage loan), small businesses are a necessity for the title insurance market.

3. The Proposed Rule Fails to Account for State Laws that Prohibit Title Insurance Discounts.

Although the rule would allow all settlement service providers to offer negotiated volume discounts, this provision is in direct contrast to many state title insurance laws that prohibit title insurance companies and agencies from discounting the title premium or offering a rebate on title insurance fees, especially in states with "all-inclusive" rates. As a result, many title companies are unable to offer consumers discounted prices under the proposed regulations.

Notably, the majority of states in the country require title insurance underwriters to file their title insurance rates with the appropriate state regulator, as well as prohibit the companies from deviating from these rates unless the planned deviations are filed with the state. This is because most state laws require state regulators to ensure that title premiums are **adequate,** non-discriminatory, and not excessive. In these circumstances, while discounted rates (like those available in a refinance transaction) are filed with the states up front, title insurance companies do not have the freedom to reduce their title insurance rates on a per transaction basis to remain competitive with other title insurance companies. Moreover, even if two title insurance companies file varying rates in the same state for the same title insurance product, the company with the higher rate is not permitted to automatically discount its title insurance.

Furthermore, most state insurance laws include anti-rebating provisions that prohibit title insurance companies and agents from making payments and/or providing discounts as an inducement for the placement of title insurance. New

York's anti-rebating provision is one example of the broad restriction on such incentives. Specifically:

> No title insurance corporation or any other person acting for or on behalf of it, shall make any rebate of any portion of the fee, premium or charge made, or pay or give to any applicant for insurance, or to any person, firm, or corporation acting as agent, representative, attorney, or employee of the owner, lessee, mortgagee or the prospective owner, lessee, or mortgagee of the real property or any interest therein, either directly or indirectly, any commission, any part of its fees or charges, or any other consideration or valuable thing, as an inducement for, or as compensation for, any title insurance business.[16]

Under this section, a title insurance company or agency in New York would be prohibited from discounting the title insurance premium, rebating a portion of the premium to the consumer (or lender), and giving any other things of value to influence the consumer's selection of a title provider. Yet, the Department proposes to allow negotiated volume discounts as a competitive technique to lower the prices for settlement services. Given these broad state-law prohibitions on title insurance discounts, we want to emphasize to HUD the restrictions under which title companies must operate. We believe the Department's proposal for negotiated discounts will have damaging effects not only on our members but for consumers who will have fewer companies from which to select title insurance services.

III. COMMENTS ON OTHER PROVISIONS OF THE PROPOSED REGULATIONS

Although the preceding section discusses ALTA's primary concerns with the proposed rule, there are other items the Association would ask the Department to consider. Moreover, ALTA would like to respond to a few issues on which HUD has specifically requested comments. Below we identify these additional issues.

A. ALTA Supports HUD Seeking Statutory Authority to Require the HUD-1 To Be Delivered Three Days Prior to Closing Only If The Statute Also Requires Lenders To Deliver Closing Documents and Instructions Four Days Before Closing.

In addition to the regulatory changes proposed by the rule, HUD identifies several items for which the Department plans to seek statutory authority. One such

[16] N.Y. Ins. § 6409(d).

item is the authority to require the HUD-1 to be provided to the borrower three days prior to closing. Although the preamble to the proposed rule includes little discussion of this legislative proposal, ALTA asks the Department to consider certain practical effects of such a three day requirement.

First, if HUD's closing script proposal were to become a reality, both the HUD-1 and the closing script (as an addendum to the HUD-1) would have to be prepared in sufficient time by the settlement agent to provide them to the borrower three days before closing. Whether or not a settlement agent can meet this deadline, however, depends on whether the loan originator provides the settlement agent with the necessary information to complete the documents. Based on current practice, settlement agents often receive the closing package shortly before closing, which would make it nearly impossible to complete the closing script and provide it to the borrower three days prior to closing. Moreover, while the proposed rule obligates the lender to supply the settlement agent with the necessary information to complete the closing script, the rule fails to prescribe a time by which the lender must transmit this information. As a result, if the Department pursues legislative authority to require the HUD-1 and its addendums to be supplied to the borrower three days prior to closing, any such statute must obligate the lender to provide the settlement agent with all necessary information to complete these documents at least four days prior to closing.

Second, the Department should consider whether the provision of the HUD-1 and closing script three days prior to closing will fulfill HUD's objective of allowing the consumer time to review the documents, understand the loan terms, and ask clarifying questions prior to closing. Often closing documents are prepared at the last minute because changes continue to occur to the mortgage, as well as the final settlement charges. Under these circumstances, it is possible that the documents provided to the consumer three days prior to closing will still not reflect final loan terms and settlement charges, which may make the disclosures useless to the consumer. Moreover, should these documents continue to change prior to closing, the consumer is likely to be more confused about the terms of settlement than had the documents never been provided to the borrower. Regardless of this argument, closers must have adequate time to complete the preparation of the closing documents before either delivery to the consumer or closing.

B. <u>HUD Should Allow Lenders the Opportunity to Cure any Violations of Tolerance Requirements</u>.

Like the Association's comments to the Department's 2002 proposed RESPA rule, ALTA continues to question whether HUD has the statutory authority to require loan originators to disclose exact third party settlement charges on the GFE. Although we will not repeat our 2002 discussion of the legislative history that supports the Association's conclusion, we emphasize that the statute only authorizes

a "good faith estimate" of the amount or range of charges for specific settlement services.[17] Yet, the proposed rule refers to the GFE as an offer, which the consumer should compare with the offers from other loan originators. By characterizing the GFE and its contents in this manner, it is ALTA's position that the settlement charges disclosed therein cease to become mere estimates, particularly when a lender could violate the regulations by exceeding the charges at closing.

Moreover, the Department's explanations provided in the rule to defend its proposal for tolerances are unconvincing. HUD states that the proposed GFE would not require lenders to itemize an exact list of settlement charges because the disclosure allows for flexibility. As an example, HUD notes that its proposal would allow the fees disclosed on the GFE to decrease at any time. This, however, is a circular argument. The Department states that its purpose for the revised GFE is to protect consumers from high settlement costs. If this is the case, the Department cannot at the same time justify its proposal for tolerances by emphasizing that settlement costs can always decrease. HUD further justifies the tolerances by suggesting that settlement fees may increase under the proposal in the case of unforeseeable circumstances. The Department, however, should recognize that a loan originator cannot rely on unforeseeable circumstances at the time it is required to disclose settlement charges on the GFE. These are events that have yet to occur, which means the lender must assume any third party settlement fee disclosed on the GFE will be subject to the tolerance limitations. While the Association appreciates the Department's efforts to distinguish its proposed tolerances from the former Section 6 of RESPA, we stand by the position ALTA expressed in its 2002 comments.

All that said, the Association recognizes that HUD believes it has statutory authority to impose tolerance limitation. Thus, should HUD include tolerances in its final rule, we support the Department's plan to allow a lender the opportunity to cure any violation of applicable tolerances. As discussed above, ALTA is concerned about the proposed rule's lack of guidance to the settlement agent in circumstances where a lender has exceeded the tolerances. From the standpoint of the settlement agent, if the agent identifies excess charges in settlement fees, which the rule makes a violation of RESPA, the agent may be unwilling to allow the transaction to close. If, however, the regulations allow the lender to refund any settlement fees in excess of the tolerance limitations within a certain period of time after closing, this should satisfy any concern and hesitation a settlement agent may have about closing the transaction.

IV. CONCLUSION

[17] See 12 U.S.C. § 2604(c).

The HUD proposal would create sweeping changes for all participants in the settlement services industry that would be most detrimental to small businesses. In this current, and potentially prolonged, decline in the real estate market, the Department should avoid causing any further disruption to the market and focus on incremental changes that can be achieved without adding to the economic downturn. This would avoid questions of statutory authority, Congressional and industry opposition, and result in meaningful changes that assist consumers in understanding loan and settlement terms and disclosures.

Moreover, the proposed rule seems to fit the refinance transaction far better than the home purchase transaction. In the former, only the interests of the borrower and lender are at issue, and virtually all of the settlement services are required for the benefit of the lender. In the home purchase transaction, there is a third party whose interests are affected – the seller – and the transfer of clear real estate title is the primary concern of both buyers and sellers. The loan, while perhaps essential, is secondary to the underlying real estate transaction. While ALTA realizes that RESPA applies to all transactions in which a federally related mortgage is involved, HUD should give serious consideration to limiting many of its changes to refinance transactions rather than applying them to purchase/sale transactions where there are likely to be significant unanticipated adverse effects that could threaten recovery of the real estate market.

Based on these concerns, ALTA suggests that HUD limit its efforts to simplifying only the GFE and HUD-1 so that comparisons can be more easily made between the documents. For instance, page one of HUD's proposed GFE provides information about the loan terms and total costs for settlement services in an understandable format. ALTA supports this type of summary page. But just as important, HUD must make fee disclosures more transparent by requiring the GFE to further break down and disclose individual title and closing service fees. This would allow consumers to know what is included within the total amount listed on the GFE summary page. This is imperative in a home purchase transaction where the buyer may require services that are not required by or of importance to the lender. It would also show what services are not required to be purchased by borrowers when sellers pay for certain services. HUD could easily accomplish this by requiring an additional page on the GFE that would be identical to page two of the HUD-1. Such a document would ensure that comparisons are clear and unambiguous.

Ultimately, ALTA appreciates HUD's consideration of these comments, and we respectfully request the Department to carefully evaluate the unintended consequences of the proposed rule. While the Association applauds HUD's attempts to simplify and clarify the mortgage loan and settlement process, we are concerned that certain aspects of the rule would discourage consumer shopping and burden our members with new forms of liability and anti-competitive pressures. In the midst of a credit crunch, ALTA accepts that there will be compliance costs with

any new regulation; however, we see no consumer benefit in implementing a rule that will complicate the settlement process and make it more difficult for small settlement service providers to compete for business and sustain their operations. If RESPA reform is to become a reality, we urge the Department to seek the proper balance between the interests of the consumer and the interests of the industry providers who serve them.

MORTGAGE BANKERS ASSOCIATION
Investing in communities

Testimony of David G. Kittle, CMB

Chairman-Elect

Mortgage Bankers Association

Before the

Subcommittee on Oversight and Investigations

Committee on Financial Services

United States House of Representatives

Hearing on

"HUD's Proposed Real Estate Settlement Procedures Act (RESPA) Rule"

September 16, 2008

Chairman Watt, Ranking Member Miller and Members of the Subcommittee, my name is David G. Kittle, CMB, and I am Chairman-Elect of the Mortgage Bankers Association (MBA).[1] Thank you for the opportunity to testify before the Subcommittee today as you consider HUD's recent proposed rulemaking under the Real Estate Settlement Procedures Act (RESPA).

Specifically, you ask about—
- Any changes you believe would be desirable to the proposed RESPA rule;
- The need for harmonization of HUD's proposed RESPA rule with the TILA rule issued by the Federal Reserve;
- Whether changes are needed to the proposed Good Faith Estimate (GFE);
- The potential challenges with implementing the proposed closing script:
- The impact of the proposed HUD rule on mortgage bankers specifically;
- Other legislative or regulatory changes to RESPA that you believe should be made; and
- Any other information or issues you believe would be beneficial to the Financial Services Committee in meeting its oversight and legislative responsibilities.

Before I begin, to introduce myself, I have been in the mortgage lending business for 30 years and am currently President and Chief Executive Officer of Principle Wholesale Lending, Inc. in Louisville, Kentucky. It is a great privilege for me to testify today before this subcommittee as a mortgage banker as well as Chairman-Elect of MBA.

In my capacity as an officer of MBA and throughout my career, I have worked with lenders of all sizes and business models from across the nation. MBA's membership of 2,400 companies spans small, medium and large mortgage bankers, as well as hundreds of small businesses in ancillary industries including law firms, technology vendors and title insurers. Also, in my work at MBA, I have been particularly involved in our organization's efforts to develop a range of approaches to simplification of the mortgage process that I believe would markedly improve it.

Most importantly, over many years, I have worked personally with thousands of consumers, answered their questions, addressed their concerns and been gratified to provide them fairly priced, sustainable loans so they and their families could realize their homeownership dreams.

Just in case there is any doubt, the MBA and I, personally, are firmly committed to improving the mortgage process for both industry and consumers alike, and we have been for a very long time. As detailed in the attached comment letter MBA filed with HUD on June 11, 2008, in response to the proposed rule, we strongly believe there is a need to update and harmonize mortgage disclosures in the interest of industry and consumers alike. For this reason, we also strongly support a comprehensive approach to mortgage reform where both HUD's RESPA disclosures and the Federal Reserve's disclosure are addressed together in a careful and coordinated manner.

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[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 370,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,400 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mortgagebankers.org.

If HUD is still determined to go forward independently, HUD's effort should be pared back to improving the forms (also as detailed in our attached comment letter). HUD's new forms should be developed in coordination with the Board so that they work in harmony with the forthcoming Truth in Lending Act (TILA) forms for the borrower. Finally, to avoid saddling borrowers with unnecessary confusion and implementation costs, HUD's and the Board's rules should be implemented on the same timeline.

Regulations impose an overly cumbersome disclosure process on the industry that increases costs. At the same time, consumers are burdened and confused by a seemingly endless pile of papers during the process, so much so that the addition of disclosures only takes them further past the point of diminishing returns.

Nonetheless, problems confronting today's mortgage borrowers reveal that while some may have made bad choices, others may have been confused about their credit costs and terms under adjustable rate mortgages, thereby entering into mortgage loans they simply did not understand. Borrowers need clarity about the terms and costs of credit that is the Board's responsibility under TILA.

RESPA, which is HUD's responsibility, is intended to provide consumers with disclosures about closing costs. While confusion about closing costs has not been as prominent an issue in the mortgage crisis, borrowers would realize significant benefits from greater transparency if the disclosures mandated under both RESPA and TILA were improved. RESPA and TILA disclosures are provided to borrowers at the same time and they should complement each other.

Viewed in context, however, this proposal comes at a time when the financial markets are more fragile than they have been in decades, as are the conditions of many lenders. Consequently, credit is also tighter than it has been in decades and, in recognition of the persistence of credit market concerns, the government recently took over the Fannie Mae and Freddie Mac (the GSEs). I would respectfully submit that this is not the time to burden the industry unnecessarily or unduly, even with the best of intentions. It is the time to carefully assess regulatory changes to help borrowers in the future and to apply them in a manner that does not worsen today's market and further tighten credit.

The Board has already issued proposed new rules under TILA and the Home Ownership and Equity Protection Act (HOEPA)[2] concerning the mortgage market generally and has announced it is now undertaking further reform efforts concerning TILA disclosures. Moreover, very recently enacted amendments to TILA under the Housing and Economic Recovery Act (HERA) necessitate additional implementation by the Board. HUD's efforts should be linked to the Board's efforts.

While there is clearly a need to improve the disclosure process, there is a right way to improve it and a wrong way. The right way is to comprehensively and carefully revise all of the federal disclosure forms under TILA and RESPA that are given to consumers. Assuring that all of these forms are not only simpler but work well together is the only real way to make certain that borrowers get a complete picture of their settlement costs and the costs of the credit so they can pick the best mortgage for themselves and their families.

[2] 73 Fed. Reg. 147 (July 30, 2008).

The wrong way is a *seriatim*, piecemeal approach where HUD first finalizes an array of changes to its disclosures and rules and later the Board finalizes its own array of changes. This not only assures differences in approach and confusion by borrowers, but it also assures increased implementation costs that are ultimately borne by borrowers. And, at the end of the day, under a piecemeal approach, government, consumers and industry will have all invested their time and money with little improvement to show for their efforts. Meanwhile, the pile of disclosures remains or even grows and the cacophony of information persists.

Only through concerted and coordinated reform of TILA disclosures regarding the costs of credit, and RESPA disclosures regarding settlement costs, can borrowers be empowered to navigate the mortgage market and protect themselves against abuse.

Looking back, MBA believes HUD pursued the wrong way by initially embarking independently on its rulemaking and then proceeding to finalize the rule in the face of these concerns. After it issued its proposal, it ignored a request from this and virtually every industry association, Federal Reserve staff and 242 Members of Congress. These commenters asked HUD to work with the Board in a careful, coordinated and comprehensive manner to improve and simplify disclosures under both TILA and RESPA. Now, HUD has not only ignored the request, but it has sent a final RESPA rule to the Office of Management and Budget for review.

Although, the final rule has not been released, our review of the proposed rule causes great concern about what the final rule might contain. As outlined below and detailed in the attached comment, rather than achieving the goal of simplicity, the proposed rule would require: a long and difficult to understand Good Faith Estimate (GFE) of loan terms and settlement costs, which would be given to borrowers before they apply for a loan; a new HUD-1 that is not readily comparable to the GFE; a lengthy "closing script" to be required at closing; as well as several controversial rule changes. The costs of all of these measures would be extremely high and many are regarded as beyond HUD's authority. Moreover, they would have unintended consequences that could ill serve consumers and the fragile mortgage and housing markets of today.

Most importantly, HUD's proposal did not demonstrate any effort to coordinate and harmonize its requirements with those currently required under TILA. In fact, the new proposed GFE discloses loan terms in a manner that is incompatible with the Board's current TILA disclosure requirements. The proposed new requirement for display of an interest rate, but not an APR, is inconsistent with the Board's current TILA requirements.

There are also many ambiguities and unanswered questions raised by the proposal as well as HUD's current RESPA rules.

MBA believes if finalized in its current form, the rule would have significant effects on businesses generally, and mortgage bankers in particular:

1) Retooling costs – The proposed rule would require extensive system changes and staff training to convert to the forms;

2) Burdensome disclosure requirements – The new requirements would take additional time and resources to fulfill, substantially increasing the costs of compliance; and

3) Increased litigation risks – Businesses would be forced to comply with a regulation that appears to conflict with other statutes and regulations, exposing businesses to liability.

For the reasons outlined below and detailed in our attached comment letter, MBA believes HUD should coordinate its efforts with the Board. If HUD is bent on going forward, HUD should pare back its effort to simplifying and improving the GFE and making it easily comparable to the HUD-1 settlement statement. This will allow consumers to effectively review their settlement costs. HUD should forego implementation of the closing script and other unwarranted rule changes at this time. Most importantly, to avoid unnecessary costs and confusion, HUD, of course, should avoid any conflicts with the Board's current and forthcoming TILA revisions, and should time implementation of any RESPA rule changes to coincide with implementation of the Board's revised TILA provisions.

BACKGROUND

Though RESPA was enacted in 1974, as early as the 1980's, the Reagan Administration is reported to have considered reform of RESPA to simplify the mortgage process. In 1992, HUD amended its RESPA rules to implement amendments to the law to permit affiliated businesses to refer customers among affiliates as long as there was disclosure and use of the affiliate was not required.[3] Also in 1992, under an opinion of the HUD Office of General Counsel and then through HUD's 1992 rule revisions, HUD required the disclosure of mortgage broker fees in table-funded transactions.[4]

In 1996, Congress required HUD and the Board to simplify and improve RESPA and the TILA disclosures and, if necessary to make recommendations for legislation to Congress to do so.[5] In 1998, as a result, HUD and the Board reported to Congress and made recommendations to establish a firmer GFE and to provide an exemption to RESPA to permit guaranteed packages of mortgage services.[6] About the same time, after the industry was confronted with litigation and consumer complaints that payments by lenders to mortgage brokers amounted to illegal kickbacks, HUD conducted a negotiated rulemaking and issued a proposed rule concerning the legality and disclosure of mortgage broker fees, which was never finalized.

In 1999 and 2001, in the face of continuing litigation concerning the legality of mortgage broker fees, HUD issued policy statements clarifying its position on the legality of broker fees also calling for improved disclosure.[7] Industry groups supported the policy statement.

In 2002, nearly six years ago, HUD proposed to reform its disclosure requirements under RESPA to: (1) provide an exemption from Section 8 of RESPA for guaranteed mortgage packages; (2) revise its good faith estimate requirements to establish tolerances for those not seeking the mortgage package exemption; and (3) improve the disclosure of mortgage broker fees. As a result of opposition to the rule from the title, mortgage brokerage and (ultimately) the mortgage lending and real estate brokerage industries, HUD withdrew its proposal in 2004.

In the summer of 2005, HUD conducted a series of seven roundtables to solicit the views of industry and consumer groups regarding RESPA reform, including small businesses.

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[3] 67 Fed. Reg. 49134 (July 29, 2002).
[4] August 14, 1992 legal opinion by Frank Keating, General Counsel, HUD.
[5] See Section 2101 of the Economic Growth and Regulatory Paperwork Reduction Act of 1996, Pub. L. No. 104-208, 110 Stat. 3009.
[6] Personal Responsibility and Work Opportunity Reconciliation Act, Pub. L. No. 104-193 (August 22, 1996).
[7] See RESPA Statement of Policy 1999-1, 64 Fed. Reg. 10080 (March 1, 1999), and Clarification of RESPA Policy Statement 1999-1, 66 Fed. Reg. 53052 (October 18, 2001).

Nearly three years later —having communicated little on the subject of reform during those years— HUD issued its proposed rule on March 14, 2008.

The proposed rule would: (1) establish a four-page standard Good Faith Estimate (GFE) form; (2) impose tolerances to limit increases in GFE estimates at closing; (3) revise requirements for disclosure of mortgage broker fees as 'the charge or credit for the interest rate chosen;" (4) make changes to the HUD-1 to facilitate comparison between GFE and HUD-1 charges; (5) establish a new script to be read to borrowers at settlement concerning final loan terms and settlement costs; (6) revise regulations to permit certain average-cost pricing and volume discounts; (7) clarify "required use" requirements to restrict disincentives to use of non-affiliates; and (8) make technical amendments to the RESPA rules.

In its proposal, HUD has also announced that it intends to seek legislative changes to: (1) authorize the HUD Secretary to impose civil money penalties for violations of Section 4 of RESPA (the Settlement Statement), Section 5 (the GFE and Special Information Booklet), Section 6 (servicing), Section 8 (kickbacks, referral fees and unearned fees), Section 9 (title insurance), and Section 10 (escrows); (2) require delivery of the HUD-1 to the borrower three days prior to closing; and (3) expand and make uniform the statute of limitations applicable to governmental and private actions under RESPA.

The proposal originally invited public comment for 60 days from the date of Federal Register publication. After receiving Congressional and other requests, HUD extended the comment period to 90 days.

A more detailed summary of the statute and the regulatory proposal is contained in Appendix E of the attached comment letter.

MBA's VIEWS ON THE RESPA PROPOSED RULE

Since HUD last issued its proposed rule in 2002,[8] the real estate industry and the mortgage system have experienced a crisis of a magnitude that was unexpected and has been unprecedented. While the crisis has resulted in pervasive dislocation and hardship for consumers and businesses alike, its benefit has been to again bring into focus what has been working in the mortgage system and what must be improved.

While MBA does not believe that the lack of transparency in the mortgage process is a principal cause of consumer difficulties, or that its improvement is the only solution, greater transparency could help stem abuses. The sheer volume and opacity of disclosures today allows abusers to hide in plain sight. As indicated, long before the current market crisis, MBA consistently supported and invested considerable resources in mortgage simplification and much greater financial literacy for consumers in the mortgage market. MBA now believes that problems in the industry are a good reason to redouble efforts in both these areas.

Greater transparency would better empower consumers to understand and pick among the range of choices available from the mortgage market based on their own financing needs and risk appetites while at the same time allowing them to shop and compare offers. This enhanced competition among mortgage lenders would also reduce costs.

[8] 67 Fed. Reg. 49134 (July 29, 2002).

MBA applauds HUD's continuing efforts at improving RESPA disclosures. At the same time, MBA also applauds the Board's announced effort to update its TILA disclosures to reflect the increased complexity of mortgage products[9] and to make improved mortgage broker disclosures part of that effort.

As recent events demonstrate, borrowers need greater clarity about the terms and costs of credit that is the Board's responsibility under TILA. RESPA, which is HUD's responsibility is intended to provide consumers with disclosures about closing costs and should accompany TILA reform. RESPA and TILA disclosures are ordinarily provided to borrowers at the same time.

Having evaluated HUD's current proposal, and the Board's current rules, it is clear that there are considerable variations between the Board's and HUD's approaches to reform. For example, HUD's proposed summary of loan terms discloses many of the terms of credit which are the Board's province under TILA but, at the same time, discloses only the note rate of the loan and not the annual percentage rate (APR) as it appears on the TILA disclosure today. This anomaly will prove confusing to both consumers and industry.

A. MBA's General and Specific Views

Considering the fragility of the market and the costs of industry changes including systems conversions necessary to accommodate new requirements, as well as the need for borrowers to better understand both the terms of their loans as well as their costs, MBA strongly believes that HUD's efforts should not be finalized until they are combined and harmonized with the Board's efforts to reform its TILA disclosures. HUD and the Board should work together to develop, reissue and finalize joint rules to simplify both the RESPA and TILA disclosures at the same time. Toward this end, MBA is furnishing, as Appendix A to the comment letter attached to the testimony, a suggested joint RESPA-TILA disclosure.

MBA believes that only through combined, comprehensive reform can consumers take advantage of better transparency and at the same time lower costs. MBA requests that both HUD and the Board involve industry and consumer advocates to help shape the proposals and that it utilize consumer testing to the maximum extent to ensure that improvements do in fact increase consumer understanding. Separate and conflicting efforts will create more confusion for consumers and increase costs for everyone involved.

If, notwithstanding the requests from this industry, Members of Congress and others, HUD determines to go forward and finalize the proposed RESPA rule independently, MBA believes the effort should be pared back considerably and put on a timeline that would match the Board's forthcoming disclosure reform efforts under TILA. Since little has changed in the ensuing period, except that the Board for now withdrew its proposal regarding mortgage broker fees (explained below), MBA calls the Subcommittee's attention to MBA's comment letter to HUD which is highlighted in this testimony. The comment letter makes the following key points:

1. HUD's summary of loan terms should be excluded from the GFE and should be issued by the Board in consultation with HUD;

[9] "The Board recognizes that [TILA] disclosures need to be updated to reflect the increased complexity of mortgage products. The Board indicated that in early 2008, it would begin testing current TILA mortgage disclosures and potential revisions to these disclosures through one-on-one interviews with consumers. The Board also indicated that it expects that this testing will identify potential improvements for the Board to propose for public comment in a separate rulemaking." 73 Fed. Reg. 1673 (January 9, 2008).

2. MBA has particular concerns about key definitions in the proposal including the proposed definitions of "mortgage broker" and "originator," which should be revised;

3. MBA supports improvement of the GFE and HUD-1 and harmonization between the forms, it therefore has strong concerns about HUD's overall disclosure approach;

4. MBA believes HUD's proposed GFE would overload the borrower with material, counter to HUD's and MBA's goal of ensuring that the consumer focuses on important information regarding mortgage costs. MBA urges HUD to work with the Board to finalize a combined RESPA-TILA form or, if it proceeds independently, to finalize a GFE form as proposed by MBA in the attached Appendix B;

5. MBA supports revision of the GFE to separately disclose mortgage broker charges;

6. While MBA appreciates HUD's efforts to facilitate shopping, this aspect of the rule should not be finalized, because of the difficulties of coordinating the concept with other laws. An alternative approach should be adopted;

7. While MBA supports methods to stem increases in fees from lenders and mortgage brokers from the time of application until settlement, it has serious concerns about HUD's proposal to limit lenders to a "zero tolerance" and to make them responsible for the charges of third-party providers. It believes retention of the "good faith" standard is consistent with the statute and that a bright line "Borrower Protection" approach should be established to help protect borrowers from fee increases;

8. The proposed changes to the HUD-1 to refer to the new GFE fail to achieve the objective of making the GFE and HUD-1 harmonious and readily comparable;

9. HUD should not implement a "closing script" to be read at closing and to be signed by the borrower;

10. MBA supports, with some modifications, HUD's proposal to clarify that lenders and brokers can use average cost pricing for settlement services within any class of transactions;

11. While MBA supports HUD's proposal to clarify the legality of volume discounts, MBA believes the proposal is too restrictive;

12. Concerning the proposed revisions to prohibitions against requiring the use of affiliates, MBA believes it would be sufficient for HUD to reaffirm that it may scrutinize discounts to ensure that they are *bona fide* rather than enact rules that would risk depriving borrowers of certain discounts altogether;

13. MBA generally supports HUD's efforts to update its RESPA regulations concerning mortgage servicing transfers and escrows and to explicitly recognize the applicability of ESIGN[10] to RESPA;

[10] On June 30, 2000, Congress enacted the ESIGN Act (15 U.S.C. §7001-7031) to facilitate the use of electronic records and signatures in interstate and foreign commerce by ensuring the validity and legal effect of contracts entered into electronically. Careful to preserve the underlying consumer protection laws governing consumers' rights to receive certain information in writing, Congress imposed special requirements on businesses that want to use electronic records or signatures in consumer transactions. Section 101(c)(1)(C)(ii) of the Act requires businesses to

14. MBA will evaluate HUD's legislative proposals as they are developed in accordance with key principles to ensure transparency and facilitate the mortgage market; and

15. MBA supports an implementation schedule that would link implementation of this rule to the Board's forthcoming TILA reform rule.

B. HUD and the Board Should Coordinate on Comprehensive RESPA-TILA Reform

RESPA and TILA are the primary laws Congress enacted to require certain mortgage information be provided to consumers.[11] They cover different aspects of the same transaction. As indicated, RESPA is intended to provide consumers information on their closing costs and TILA is intended to provide consumers information on the terms and costs of credit. RESPA and TILA disclosures are provided to most borrowers at the same time during the mortgage process.

Better information on both credit terms and loan costs, as well as better information on mortgage broker compensation, would greatly empower borrowers and protect them from abuse. The need for improvements in both understanding credit and settlement costs strongly militates in favor of both HUD and the Board working together in the reform process so that both RESPA and TILA disclosures are compatible.

Piecemeal, sequential or *seriatim* reform of the RESPA disclosures, however, followed by reform of the TILA disclosures, would be extremely costly to businesses both small and large, and ultimately to consumers. New disclosures along the lines HUD proposed will require substantial retooling of systems and considerable expenses for training, compliance and staffing. Changes to TILA are expected to result in similar costs. Since the mortgage crisis has led to tightened and more costly credit for lenders and borrowers alike, these very considerable expenses would occur at just the time that the industry and consumers can least afford them. Moreover, if the efforts of the agencies are not compatible, they will greatly confuse consumers and increase the costs to industry and consumers even more.

HUD's own Regulatory Flexibility Analysis estimates that the total one-time costs to the lending and settlement industries of the new GFE and HUD-1 alone will be $570 million, $390 million of which are estimated to be borne by small business.[12] HUD estimates that the total recurring costs are estimated to be $1.231 billion annually or $98.74 per loan. While MBA believes these costs are underestimates, even if they were accurate, the costs of TILA reform, following after these costs are incurred, can be expected to result in costs of similar size for retooling, retraining, re-staffing and other costs to the industry.[13] If, on the other hand, RESPA and TILA changes were accomplished together, it is reasonable to anticipate that economies could result in lower costs to implement both sets of reforms.

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obtain from consumers electronic consent or confirmation to receive information electronically that a law requires to be in writing. The Act went into effect in October 2000.

[11] The Truth in Lending Act (TILA) covers credit in addition to mortgages: "It is the purpose of this subchapter to assure a meaningful disclosure of credit terms available to him and avoid the uninformed use of credit, and to protect the consumer against inaccurate and unfair credit billing and credit card practices" (TILA §102, 15 U.S.C. §1601).

[12] 73 Fed. Reg. 14102 (March 14, 2008).

[13] Schnare, Ann B., The Estimated Costs of HUD's Proposed RESPA Regulations, National Association of Realtors, (June 3, 2008).

In any event, hasty efforts at mortgage reform should not be justified based on current market difficulties. While it is clear that borrowers are experiencing higher default and foreclosure rates today than they have in recent years, the great majority of loans and borrowers in the nonprime market are performing well, as are the vast majority of prime loans. The area of greatest concern has been nonprime adjustable rate mortgage (ARM) loans and particularly hybrid ARMs (which employ an extended introductory rate period with an adjustable rate feature at the end of the introductory period) which are generally no longer available in today's market to these borrowers. While there are concerns that steering by mortgage brokers may have been part of the problem, there is no apparent evidence that closing costs have been a major aspect of it.[14]

It must also be borne in mind that as mortgage applications have risen over the last two decades, so too have the percentage of families realizing – and successfully sustaining – the dream of homeownership. This is due to several factors including lower interest rates (which are at historically low levels – even today), risk-based pricing and a host of industry efforts and innovations. According to the Board's Flow of Funds data,[15] the value of residential real estate assets owned by households has increased from $10.4 trillion in 1999 to $20.1 trillion as of the first quarter of 2007, and aggregate homeowner's equity now is $9.6 trillion. Unnecessarily increased costs that might stem from unwise reforms should not be allowed to undermine the objective of sustainable homeownership.

C. If HUD Goes Forward Independently

Once again, MBA strongly reiterates that HUD and the Board should work together in the interests of industry and consumer alike. However, if HUD decides to finalize the proposed rule without such coordination, MBA believes the rule should be pared down and several significant changes should be made before a final rule is published.

1. HUD's summary of loan terms should be excluded from the GFE and should be issued by the Board in consultation with HUD.

MBA strongly believes that while a "Summary of Your Loan Terms" could be very useful to provide borrower's key information to better understand mortgages and to shop among them, it should not be part of the HUD proposal and should be developed and issued by the Board. Were HUD and the Board to separately issue such summaries, the efforts would be duplicative and confusing.

While HUD's proposed summary includes "adjusted origination charges," "charges for other settlement services" and "total estimated settlement charges," the summary mainly concerns points relevant to credit costs and terms that are the Board's province.

Notably, while HUD's proposed summary displays the "initial interest rate," it does not include the "annual percentage rate" or "APR" or the Finance Charge" and the "Amount Financed." Although MBA believes these terms themselves cause confusion, the Truth in Lending Act requires their use at this time. Also, by dealing with the matters of "balloon payments" and "prepayment penalties," the summary is unnecessarily repetitious of the TILA disclosure. The

[14] See 73 Fed. Reg. 1698-1700 (January 9, 2007).
[15] The Board's Flow of Funds data may be viewed at the following Website: http://www.federalreserve.gov/releases/z1/current/default htm.

Board also should issue the summary to assure its consistency with forthcoming TILA disclosures as well as current ones.

2. Definitions – MBA has particular concerns about key definitions in the proposal including the proposed definitions of "mortgage broker" and "originator," which should be revised.

MBA does not support changes in the definition of mortgage broker to include an "intermediary" and it does not support calling both lenders and brokers "originators." While MBA understands that some advocates for the mortgage brokerage industry argue that a "level playing field" requires this blurring of the roles of lenders and brokers respectively, the fact is that the players and their functions are substantively different. This proposed nomenclature blurs these distinctions and obfuscates the differing regulatory needs of consumers regarding lenders and brokers.[16]

To clarify this and other related issues, MBA has recently published the attached paper "*Mortgage Bankers and Mortgage Brokers: Distinct Businesses Warranting Distinct Regulation*" which is attached as Appendix D to MBA's comment letter.[17]

The paper points out that mortgage brokers are middlemen that facilitate or make arrangements for loans and that lenders, on the other hand, incur risk and lend money. Consumers perceive brokers and lenders differently. Consumers regard mortgage brokers as shopping for them and ordinarily cease their own shopping when they deal with them, ceding the shopping to the broker. In contrast, consumers regard lenders (and their employees and agents) as providers of loan products amongst whom they shop and compare.

Because mortgage brokers are regarded as shopping for borrowers, they present a much greater risk of steering consumers to a higher rate loan in return for a larger fee. Accordingly, MBA believes it is appropriate for brokers, to tell borrowers the compensation they receive from lenders. MBA does not believe that lenders or their exclusive agents warrant the same treatment because borrowers do not perceive them the same and they do not present the same risks.

3. MBA supports improvement of the GFE and HUD-1 and harmonization between the forms, it therefore has strong concerns about HUD's overall disclosure approach.

MBA appreciates HUD's effort to create a comprehensive GFE document to help the borrower shop and better understand the mortgage process. Although MBA understands that the first page is intended to be a summary, and the second page a list of closing costs, MBA believes the resultant document is far too long and would overload the borrower with material that ultimately would be ignored and therefore would be counterproductive to HUD's and MBA's own consumer protection objectives.[18]

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[16] A comment letter transmitted on June 4, 2008 from the Federal Deposit Insurance Corporation to HUD in regards to the proposed rule objects to this provision of the proposal because it blurs the distinction between brokers and bankers.
[17] The paper is also available on the Web at the following address: http://www.mortgagelenders.org/files/News/InternalResource/62646_Paper.pdf.
[18] A comment letter transmitted on June 4, 2008 to HUD from the Federal Deposit Insurance Corporation indicates that in light of its own testing of consumers, it has the same concern.

The proposed changes to the HUD-1, while also appreciated, also fall short of making the GFE and HUD-1 correspond, necessitating the use of a "closing script" to be read by the closing agent and signed by the borrower. MBA believes that a better approach would be to make the GFE more closely correspond to the HUD-1, so that the consumer could easily compare the two documents, eliminating the need for the closing script altogether. MBA's proposed GFE and HUD-1 forms appended to the comment letter do more closely correspond and should be adopted by HUD if it moves forward independently.

4. MBA believes HUD's proposed GFE would overload the borrower with material, counter to HUD's and MBA's goal of ensuring that the consumer focuses on important information regarding mortgage costs. MBA urges HUD to work with the Board to finalize a combined RESPA-TILA form or, if it proceeds independently, to finalize a GFE form along the lines of the Appendix B of the attached comment letter.

As indicated, MBA strongly supports a combined and coordinated effort by HUD and the Federal Reserve to develop and implement a joint GFE-TILA disclosure. For this purpose, industry representatives –including MBA members– developed the two-page form appended to the comment letter with the first page displaying the settlement costs and the second page displaying the costs of credit for a consumer's mortgage.

If HUD goes forward to finalize the GFE independently, MBA urges HUD to use the RESPA related portions of the forms. MBA provided an earlier version of the form to HUD which HUD critiqued in its Regulatory Flexibility Analysis.[19] These forms have been revised to address those comments and this subject is discussed in MBA's comment letter.

Also, while MBA generally supports the grouping of the amount or ranges of specific services on the GFE in a manner that is comprehensible and comparable, the form itself should be modified so it is mainly a list of charges with minimal supplementary material, as is the MBA form in Appendix B to the comment letter. MBA believes most of the material on the form, except the costs, should be moved to explanatory materials, such as the Special Information Booklet.

MBA maintains that the form appended to the comment letter is much more useful than HUD's proposed GFE. The recommended form is much shorter and was developed by those who make mortgage loans and day-in and day-out are presented with consumers' questions. It is also readily comparable to the revised HUD-1, also appended to the comment letter, and also developed by MBA and presented to HUD. MBA believes the use of these comparable forms throughout the mortgage process at shopping, at or following application, following underwriting and at and a day before closing would eliminate the need for the closing script and reduce costs to small and large businesses.

While MBA believes that there will be retooling costs associated with implementation of its shorter GFE and HUD-1, it believes that its forms will be easier to implement and easier for borrowers to understand, These differences will translate into lower initial, and much lower recurring, costs for businesses large and small and ultimately borrowers.

5. MBA supports revision of the GFE to separately disclose mortgage broker charges and complement mortgage broker fee agreements.

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[19] Pages 4-8 through 4-11 and 4-19 through 4-20, Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis, FR-5180-P-01, Proposed Rule to Improve the Process of Obtaining Mortgages and Reduce Consumer Costs, Department of Housing and Urban Development (March 2008).

MBA has long supported a straightforward disclosure of mortgage broker fees as the best way to protect consumers and finally resolve this issue that has bedeviled the industry and consumers for years. Recently, legislators have sought to limit or eliminate yield spread premiums (YSPs). While MBA strongly supports the legality of YSPs and other fees paid by lenders to permit consumers the option of "building their closing costs into their rate and monthly payments," MBA believes that clear disclosure is essential. Disclosure can help assure that these payments do not simply augment borrowers' costs, unbeknownst to them, and also help stem steering of consumers by mortgage brokers to higher rate products.
The Board originally proposed under its Homeownership and Equity Protection Act rules to require brokers to enter into agreements with consumers spelling out the compensation they were to be paid by the lender prior to any such payment along with a description of the broker's incentives. Although this proposal was withdrawn pending further review as part of the forthcoming TILA review, the OCC now requires a similar upfront disclosure. In light of such agreements, MBA believes there should be a place on the GFE and HUD-1 to reflect these disclosures.

HUD's proposed GFE and HUD-1 do not require a clear enough disclosure of lender payments to mortgage brokers nor do they reference any earlier agreement. Instead, HUD would revise the requirement for disclosure of YSPs from lenders to mortgage brokers so that it would be described as "a charge or credit for the interest rate chosen." This amount would be subtracted from the lender and brokers' "service charge" to arrive at the "adjusted origination charge." MBA believes the costs occasioned by the adoption of this new terminology for mortgage broker fees will be enormous but its benefits to elucidate consumers will be few.

While MBA appreciates HUD's efforts to clarify the function of a YSP in relation to the interest rate, MBA believes that this could be accomplished without creating confusing new terminology for broker fees. Also, some brokers may be paid on a basis other than a loan's interest rate and HUD's forms do not contemplate that possibility.

In contrast, MBA's proposed GFE appended to MBA's comment discloses to the borrower in plain English the total compensation for the broker's services and the amounts paid by the lender to the broker on the borrower's behalf. It also references any agreement and indicates that the amounts paid to the broker by the lender are paid by the borrower through the loan's interest rate and monthly payment.

Based on the preamble, the proposed rule and the Regulatory Impact Analysis,[20] MBA understands that HUD's approach to disclosure is shaped by concerns from mortgage brokerage industry advocates and the Federal Trade Commission (FTC) that the form should provide a "level playing field" between brokers and lenders. MBA believes that these assertions are incorrectly premised and obfuscate or do not fully comprehend the differing functions and the differing consumer expectations of brokers and lenders respectively. This approach also does not appropriately address the consequently greater threat of steering by mortgage brokers. Notably, the Federal Deposit Insurance Corporation (FDIC) does not appear to share the FDIC's approach.[21]

[20] See 73 Fed. Reg. 14030 (March 14, 2008).
[21] Both the Board, prior withdrawal of its HOEPA proposal, and the FDIC have supported different approaches as shown in the HOEPA proposed rule and the comment letter on the HUD proposal from the FDIC.

As indicated, lenders and brokers perform distinct functions in the marketplace and are perceived differently by consumers. As explained in the attached paper at Appendix D to the comment letter, they are not the same players; they do not have the same role, and applying the same rules to them is ill-advised.

Specifically, considering that consumers regard brokers as middlemen who comparison shop for them, it is wholly appropriate for the consumer to know if the broker is also receiving a fee from the lender based on the consumer's choice of a higher rate. Armed with compensation information, and other information on the relationship between the interest rate and settlement costs, the consumer can make an informed choice and avoid steering and abuse.

Requiring separate disclosures of mortgage lender fees and mortgage broker compensation is consistent with HUD's current requirements. HUD's own Statements of Policy issued in 1999 and 2001[22] provide that mortgage brokers must provide distinct goods, facilities or services to justify compensation and such compensation must be reasonably related to the value of such goods, facilities and services. The Policy Statements and HUD's rules direct separate disclosure of mortgage broker fees.

MBA agrees with these directives and believes that broker fees must be separately itemized, and specifically labeled, so that consumers and regulators are able to discern whether the compensation paid to a mortgage broker is in fact reasonably related to the goods, services and facilities provided. Any disclosure approach that combines broker and lender compensation would undermine HUD's own analysis of the legality of broker fees. Therefore, by separately disclosing broker and lender compensation, MBA's proposed forms are consistent with HUD's longstanding legal interpretations in this area.

Finally, MBA notes that HUD spends considerable time in the preamble to its proposal discussing the consumer testing of its forms in general and of the broker disclosure in particular. The purpose of this testing though was to avoid borrowers incorrectly selecting lenders' versus brokers' loan offers. This approach, however, incorrectly assumes that there are no differences between brokers and lenders. Considering all the distinctions identified in MBA's paper in Appendix D to the comment letter, MBA believes that borrowers need to understand both the functions and fees of lenders and brokers respectively. The tests conducted by HUD are not relevant to the panoply of concerns surrounding these issues. MBA strongly supports testing of the forms it proposes which make the respective fees clear and also reference any mortgage broker fee agreement.

6. While MBA appreciates HUD's efforts to facilitate shopping, this aspect of the rule should not be finalized because of the difficulties of coordinating the concept with other laws. An alternative approach should be adopted (as discussed in 7 below).

As detailed in the comment letter, while MBA appreciates HUD's efforts to facilitate shopping, the fashioning of a new "GFE application" to elicit a binding GFE raises significant regulatory concerns and statutory questions.

The matter of bait and switch in consumer shopping could be better resolved by empowering consumers with a new "shopping tool" developed by HUD and the Board, along the lines proposed at Appendix C of the comment letter that would elicit offers from lenders and mortgage brokers. As discussed in greater detail in the comment letter, the matter of stopping

[22] 64 Fed. Reg. 10080 (March 1, 1999); 66 Fed. Reg. 53,052 (October 18, 2001).

unwarranted payment shock from the time of application to the time of closing can be addressed without changing the definition of "application."

Under HUD's proposal, the definition of "mortgage application" currently found in RESPA's implementing regulation would be replaced with two new definitions that, in effect, would bifurcate the mortgage application process into two distinct phases - the "GFE application" phase and the "mortgage application" phase. The impact of this redefinition has repercussions that extend well beyond RESPA, and may significantly alter legal and regulatory responsibilities under other laws and/or engender great confusion.

Specifically, changes in the definition of "application" would impact TILA and "Regulation Z,"[23] the Equal Credit Opportunity Act (ECOA) and "Regulation B,"[24] the Home Mortgage Disclosure Act (HMDA) and "Regulation C,"[25] the Fair Credit Reporting Act (FCRA) rules, and Section 311 of the Fair and Accurate Credit Transactions Act of 2003 (FACTA)[26] concerning the risk-based pricing notice.

But MBA does not believe these changes are necessary. Variations in costs from the time a borrower shops until the time they actually apply with a particular lender or mortgage broker is a different matter from closing cost shock at the time of settlement, where actual closing costs significantly vary from costs estimated at the time of mortgage application. The former, in MBA's view, is less of a problem and does not warrant revising the definition of application considering the foregoing regulatory concerns.

Many consumers today effectively shop among mortgage lenders. In order to further facilitate shopping by others among lenders and brokers, MBA supports the establishment of a new shopping tool to be developed by HUD and the Board, along the lines proposed by some members of MBA, and attached as Appendix C to the comment letter. Such a tool would elicit offers from lenders and mortgage brokers in the form of a non-binding GFE at Appendix A of the attached comment letter. The market would respond, as it does today, with relatively firm offers and the borrower could use the tool to narrow its search.

There is also some concern that shopping through a series of applications would adversely affect borrower's credit ratings. This concern would be obviated by the use of a shopping tool and non-binding GFEs.

Finally, going forward, HUD and the Board should make clear in informational materials that prices alone need not be determinative of a consumer's choice of a lender or mortgage broker. Borrowers do and should consider the quality of services provided, including, but not limited to, the particular lender's capacity and competence to provide responsive and prompt service to facilitate a timely, efficient and high quality lending experience.

7. While MBA supports methods to stem increases in fees from lenders and mortgage brokers from the time of application until settlement, it has serious concerns about HUD's proposal to limit lenders to a "zero tolerance" and to make them responsible for the charges of third-party providers. It believes retention of the "good faith" standard is

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[23] 12 C.F.R. § 226.
[24] See *Federal Reserve Board Regulation B Official Staff Interpretations*, 12 C.F.R. § 202.2(f), Supp. I, comment 2.
[25] 12 C.F.R. § 203.2(b).
[26] Pub. L. No. 108-159 (December 4, 2003).

consistent with the statute and that a bright line borrower protection approach should be established to help protect borrowers from fee increases.

While MBA supports greater protection for consumers against significant unjustified cost increases from the GFE at time of loan application to closing, it does not believe that the establishment of a zero tolerance for lender or broker fees is justifiable under RESPA or that a 10 percent tolerance on certain third party charges required by the lender or broker, as detailed below, is the best approach.

While MBA opposes unjustified increases in settlement costs at closing, the establishment of tolerances, in general, and restriction to a zero tolerance, in particular, for lender fees are legally questionable under RESPA. Section 5 of RESPA requires a "good faith estimate of the amount or range of charges for specific settlement services the borrower is likely to incur in connection with the settlement as prescribed by the Secretary."[27] While HUD asserts that the basis for its ability to impose tolerances is grounded in its ability to define the term "good faith," MBA does not believe that – considering the structure or legislative history of the statute – there is clear basis for tolerances generally and particularly a "zero tolerance."[28]

MBA does not believe that, as a general matter, lenders can or should be held responsible for the costs of third parties when lenders have no ability to control their costs. As more fully discussed below, the current proposal for volume discounts will not facilitate pricing arrangements that will be beneficial to the consumer. Lenders will not enter into volume discount arrangements if doing so causes them to face additional liability. MBA also believes that the establishment of a 10 percent tolerance overall on third-party charges recommended by

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[27] 12 U.S.C. § 2604(c).

[28] The proposed amendments to the GFE are inconsistent with RESPA insofar as those amendments would impose tolerances or other specific standards for the accuracy of the GFE disclosure. The RESPA statute requires the lender to provide "a good faith *estimate* of the amount or range of charges for specific settlement services the borrower is likely to incur in connection with the settlement as prescribed by the Secretary." 12 USC 2604(c) (emphasis added). This is a requirement for an estimate of the settlement charges, not a requirement that these charges be disclosed with exact accuracy. Congress separately provided in RESPA for a final settlement statement for the charges actually imposed. 12 USC 2603. This requirement for a final settlement statement differs markedly from the GFE requirement by not stating that the disclosures could be provided as estimates. Because Congress provided separately for a final statement of settlement charges (in Section 4 of both the original RESPA and the current RESPA), and a "good faith estimate" of the settlement charges to be provided at the beginning of the loan application process, it seems clear that Congress did not contemplate that the GFE would be absolutely accurate.

The amendments at the enactment of RESPA are also instructive. The original RESPA statute stated that is was "the duty of the lender," when making the advance disclosure of settlement charges, "to obtain or cause to be obtained from persons who provide or will provide services in connection with such settlement the amount of each charge they intend to make." 12 USC 2605 (1974 version). Congress deleted this duty in its amendment to RESPA in 1976 when Congress added the formal GFE requirement. The RESPA statute has not changed in that regard since 1976 and still does not impose an affirmative duty on the lender to enter into binding relationships with third parties regarding the amount of such third parties' fees. While a lender must make a good faith effort to obtain accurate information as to the amounts of third party charges, that is quite different from a requirement that the disclosure of those amounts be accurate within regulatorily-specified tolerances.

Comparing RESPA to TILA, Congress expressly included accuracy standards and tolerances into TILA. See, for example, 15 USC 1605(f) and 1649(a)(3) (each providing accuracy tolerances for finance charges), and 15 USC 1606(c) (providing tolerances for the disclosure of the annual percentage rate). In contrast, Congress did not impose or imply accuracy standards for GFE's.

Therefore, we believe that HUD's attempt to impose strict accuracy standards for the GFE is inconsistent with RESPA itself. Any such action by HUD would be in excess of HUD's statutory jurisdiction and authority, and a reviewing court therefore should hold such action to be unlawful and set it aside under the APA. 5 USC 706(2).

the lender will likely prove counterproductive as long as the lender is held liable for violations of the tolerances. Lenders will simply not have the incentive to make any recommendations to the consumer of beneficial services.

Additionally, MBA believes the establishment of a tolerance for government recording and transfer charges is unwarranted and presents unnecessary risks to lenders and to mortgage brokers.

While MBA notes that HUD has provided relief from the tolerances for unforeseeable circumstances, including acts of God and exceptions for other circumstances, MBA believes that these exceptions are too narrow considering the applicable statutory requirements, as detailed in the attached comment letter.

MBA believes that the current regulations are more consistent with the current statute in requiring that estimates must be made in "good faith" and bear a "reasonable relationship" to the charge a borrower is likely to pay at settlement.[29] The rules should not require a lender to show that all increases are unforeseeable. What should be required is that the lender make estimates based on information known to him in "good faith" at the time the estimates are made.

Finally, MBA does not believe there is a legal basis for RESPA rules requiring that when a loan application is rejected, and the tolerances are inapplicable, the borrower must be notified within one day. A one-day requirement is also unreasonable considering other workload constraints and, in MBA's view, it will present a particular hardship to small mortgage lenders and brokers. Moreover, before the rule is finalized, it must be harmonized with other provisions of law governing notice of denial (e.g., ECOA).

As indicated, MBA believes a better approach under the current statute, as detailed in the comment letter, would be to apply the current regulatory standard for good faith estimates at 24 C.F.R. § 3500.7 which provides:

> *Each such estimate must be made in good faith and bear a reasonable relationship to the charge a borrower is likely to be required to pay at settlement, and must be based upon experience in the locality of the mortgaged property. As to each charge with respect to which the lender requires a particular settlement service provider to be used, the lender shall make its estimate based upon the lender's knowledge of the amounts charged by such provider.*

The rules would then establish that HUD and other federal and state regulators would scrutinize lenders' good faith estimates for compliance unless lenders' and brokers' good faith estimates were in conformity with the Borrower Protection approach described below.

Under this approach, lenders and brokers would be deemed to be in good faith for any mortgage where (1) their own fees were no more than five percent greater at closing than estimated on the GFE at time of application and (2) estimated third party charges of providers required and selected or recommended by the originator were no more than 10 percent greater overall than estimated on the GFE.

When the borrower is ready to apply for a mortgage, he or she would do so. The lender or broker would then provide a GFE either by delivering the good faith estimate, or by placing it in

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[29] 24 C.F.R. § 3500.7(c).

the mail to the loan applicant, not later than three business days after the application is received or prepared.

The GFE would be provided at no cost, except possibly for the cost of the credit report. MBA is mindful that the Board has proposed to require the early TILA disclosure without any significant fees and it supports the provision of a combined RESPA-TILA disclosure. However, in instances where the borrower wishes expedited treatment, the borrower should be allowed to provide a fee if he or she chooses an appraisal or a rate lock to expedite closing or to lock-in a rate. The ability to lock-in should not be unwittingly prevented under any new rules.

The GFE must be provided in good faith and would be subject to enhanced regulatory review. The foregoing five percent leeway on lender fees (including discount points and any charge for when a rate is locked) and a 10 percent overall window of certain costs (including title, appraisals, and required services the lender or broker selects or recommends such as pest inspections) on the GFE would apply to lenders and mortgage brokers to assure that they meet the good faith standard. Under this approach, fee increases that exceed these standards could be scrutinized by HUD or another applicable state or federal regulator to determine whether they are in good faith or whether they were not.

8. The proposed changes to the HUD-1 to refer to the new GFE fail to achieve the objective of making the GFE and HUD-1 harmonious and readily comparable.

While laudable, MBA does not believe that the changes to the HUD-1, in the form of relatively minor revisions and references to the GFE, are sufficient to make the forms truly comparable for the consumer. In fact, MBA believes that the introduction of the new closing script, which is intended to describe the relationship of the costs and terms on the GFE to those on the HUD-1, is at least in part an admission that the forms are not easily comparable. Considering that HUD's cost estimates for implementation of the GFE and HUD-1 forms are based on the comparability of these forms, MBA is convinced that these cost estimates are far too low.[30]

9. HUD should not implement a "closing script" to be read at closing and to be signed by the borrower.

As detailed in the comment letter, MBA does not believe that implementation of the closing scripts proposed by HUD, as an addendum to the HUD-1 or HUD-1A, is advisable. MBA believes its implementation would raise legal concerns, be too costly, provide little benefit to the consumer at closing and raise significant operational concerns. Moreover, the script itself is concerned with both loan terms and settlement costs and as such should await the involvement of the Board as part of comprehensive RESPA-TILA reform, if it is to be implemented at all.

Just as important, MBA believes that the script will add unnecessary costs to the closing process. HUD itself estimates that the script will add 45 minutes of additional time per closing and estimates that cost at $54 (derived from a $150,000 salary). HUD also says the costs in a normal year (based on 12.5 million originations) would be an estimated $676 million. It is not apparent, however, in reaching what MBA regards as an unusually low estimate, HUD fully considered all costs including the additional time for the lender, broker and others to assist in developing the script. There is also no apparent consideration of the considerable costs to borrowers considering the time the borrower must invest in this effort, e.g. lost wages.

[30] 73 Fed. Reg. 14115-14116.

For the consumer, closing is far too late to focus on a comparison of estimated and final loan terms and closing costs. It would be far better for the consumer to be provided a HUD-1, and a TILA disclosure prior to closing that was readily comparable to the GFE. Prior to closing, a consumer can question the lender or broker about charges and determine whether he or she will proceed with the loan.

Current RESPA regulations[31] permit the borrower to inspect the HUD-1 or HUD-1A settlement statement the business day immediately prior to settlement but the rules only require review of items that are known to the settlement agent at the time of inspection. Over the past few years, MBA, the American Land Title Association (ALTA) and the American Escrow Association (AEA) have been working together to develop uniform closing instructions. In their current form, these procedures, while not yet finalized, would, in part, enable borrowers to receive a complete HUD-1 a day before closing. MBA believes that, enhanced by a GFE that is truly comparable to the HUD-1, this effort holds far greater promise than the closing script to timely inform borrowers of closing costs and facilitate comparison with the GFE.

Finally, use of such a script would present logistical problems in eMortgage transactions and in states where escrow closings are prevalent. The use of the script will either make these transactions unworkable and/or simply increase the paper required for borrower review. Also, considering that settlement agents must read the script and will be expected to answer questions, the script's use may be impossible in states where there are statutes prohibiting the unauthorized practice of law.

10. MBA commends, with some modifications, HUD's proposal to clarify that lenders and brokers can use average cost pricing for settlement services within any class of transactions.

MBA commends HUD's proposal to exert its authority under Section 19 of RESPA to clarify that lenders and brokers can use average cost pricing for settlement services, with some clarifications and modifications. MBA has long sought explicit clarification of the legality of average cost pricing, not to increase industry profits but to facilitate pricing arrangements to reduce operational and compliance costs, and streamline operations, all of which will result in lower costs to consumers. Average cost pricing methodologies permit tiered pricing arrangements where the average prices for third party services purchased in volume are lower than the prices for services purchased individually. These benefits are passed on to consumers in the market. Explicitly permitting these arrangements reduces legal risks resulting from requirements for precise price calculations.

MBA believes that with some modifications and clarifications, detailed in the comment letter, considering the benefits of average cost pricing, this proposal should be finalized even if the entire rule is not. In such event, MBA respectfully requests that HUD issue a policy statement or an interpretive rule for this purpose. For example, MBA believes that before this provision is finalized under a rule or an interpretative rule, the rule should be clarified to give maximum latitude to the lender to define a "class of transactions." Specifically, the lender should have latitude to broadly define a class based on type of service, type of property, loan type and/or geographic region. The standard should be "a reasonably similar class of transactions" as defined by the lender. This approach would give the lender discretion to identify transactions such as valuations in a particular county or the subset of semi-detached homes in such county.

[31] 24 C.F.R. § 3500.10(a)

Likewise, the lender should have latitude to define an "average period" and the "average price" as long as the approach is "reasonable."

Finally, the documentation requirements should be revised to ensure that they are flexible and do not impede use of this provision by requiring unnecessarily burdensome documentation. The documentation should not be required to be retained to demonstrate "accuracy" but to support the lender's determinations.

11. While MBA commends HUD's proposal to clarify the legality of volume discounts, MBA believes the proposal is too restrictive.

MBA also commends HUD's proposal under Section 19 of RESPA to clarify that volume discounts are not prohibited, but does not believe it goes far enough. MBA respectfully directs the subcommittee, to the attached comment letter for ways to make these provisions operate more effectively. If it is modified, MBA believes that it also should be issued as an interpretative rule or clarification whether or not HUD goes forward with this rulemaking.

Negotiated discount arrangements for services and materials result in lower costs to consumers and are therefore consistent with RESPA's purposes of lowering settlement costs. These arrangements achieve this objective in other industries, such as in the automobile industry where parts are ordered through volume arrangements. MBA does not believe RESPA was intended to or should impede similar discounting in the settlement services industry.

Nevertheless, by also including a requirement that no more than the reduced price can be charged to the borrower, MBA believes that there will be little incentive for lenders to enter into discount arrangements. Scrutiny to ensure that each and every dollar of discount is passed on to the consumer presents regulatory risks and will make the exception uninviting. Moreover, such a restriction is unnecessary. Market competition will result in the consumer receiving the benefit of discounts. If HUD is insistent about maintaining this provision, at the very least, HUD should make clear that "average cost pricing" can be employed in conjunction with volume discounts. Under such an approach, it would be acceptable for the average price to be charged to the borrower, if permissible under the rules, rather than the fully discounted price.

12. Concerning the proposed revisions to prohibitions against requiring the use of affiliates, MBA believes it would be sufficient for HUD to reaffirm that it may scrutinize discounts to ensure that they are *bona fide* rather than depriving borrowers of certain discounts altogether.

HUD proposes to change the definition of "required use" so an economic disincentive where a consumer will pay a higher price if it fails to purchase a settlement service from an affiliated provider would be as problematic under RESPA as a requirement that a consumer choose a particular provider. The proposed rule indicates that it is particularly directed to homebuilder affiliates but covers other affiliate situations.

MBA believes that the proposal in this area is too broad and may result in depriving borrowers of discounts that may indeed be *bona fide.* MBA believes it would be sufficient for HUD to indicate that under its current rules it may scrutinize discounts to assure they are *bona fide* rather than risking depriving borrowers of discounts altogether, as indicated in the attached comment letter.

13. MBA generally supports HUD's efforts to update its RESPA regulations concerning mortgage servicing transfers and escrows and to explicitly recognize the applicability of ESIGN to RESPA.

MBA supports those clarifications that will conform the rules to current law and practice and thereby alleviate confusion in the real estate finance industry and among the consumers it serves, thereby reducing costs to companies large and small.

14. MBA will evaluate HUD's legislative proposals as they are developed in accordance with key principles to ensure transparency and facilitate the mortgage market.

In its proposal, HUD announced that it intends to seek legislative changes to: (1) authorize the Secretary to impose civil money penalties for violations of Section 4 of RESPA (the Settlement Statement), Section 5 (the GFE and Special Information Booklet), Section 6 (servicing), Section 8 (kickbacks, referral fees and unearned fees), Section 9 (title insurance), and Section 10 (escrows); (2) require delivery of the HUD-1 to the borrower three days prior to closing; and (3) expand and make uniform the statute of limitations applicable to governmental and private actions under RESPA.

There currently are some provisions under Sections 6, 8, 9 and 10 of RESPA to enforce those provisions but no appreciable enforcement authority exists under Sections 4 and 5. Nevertheless, state and federal regulators under a variety of laws do enforce these requirements. For this reason, as the proposals are developed, MBA will evaluate them carefully in the context of other authorities, including those under TILA, and the following principles:

- Disclosures should be streamlined and greatly simplified and uniform throughout the nation; terms that are not consumer friendly should be replaced with terms that are simple and understandable;
- Disclosures should be binding as early in the process as possible, considering that during the mortgage process information is developed and circumstances can change;
- The timing of disclosures should not result in undue delay for borrowers to receive needed credit;
- The process should facilitate competition to lower costs as well as the provision of high quality services;
- Borrowers and regulators should be appropriately empowered to prevent abuses;
- Lenders should have a reasonable opportunity to cure errors prior to litigation; and
- Remedies for errors should not result in unduly increased costs for all consumers.

15. MBA supports an implementation schedule that would link implementation of this rule to the Board's forthcoming TILA reform rule.

Although, MBA strongly prefers combination of the TILA and RESPA efforts, as indicated, MBA believes the objective of minimizing costs can, to some extent, be achieved through an extended implementation period if HUD goes forward independently. In such event, MBA recommends that the implementation period for new forms and any aspect of the rule that requires retooling, systems changes or other significant costs should extend to 18 months after the rule's effective date or until the end of the implementation period for the Board's new rule, whichever is later.

CONCLUSION

MBA has long supported efforts to make the mortgage process simpler, clearer and more transparent for consumers. But HUD's proposal raises serious issues and it is not simplification. Moreover, it comes at a time when the market is fragile and neither industry nor consumers should be forced to bear unnecessary and undue costs. If we are to proceed with mortgage reform, it is imperative that we do it right. Considering these points, common sense dictates that HUD and the Board work together to reform all of the federal disclosures to borrowers under RESPA and TILA. If HUD goes forward independently, the rule should be pared down to simplifying the RESPA forms. HUD should consult with the Board so the changes resulting from HUD's and the Board's efforts are harmonious, work for borrowers and are implemented at the same time to avoid confusion and unnecessary costs.

On behalf of MBA, I greatly appreciate the opportunity to present our views on these important issues. I look forward to your questions.

ATTACHMENT

MBA's June 11, 2008 Comment Letter to HUD in Response to

HUD's Proposed RESPA Rule, Docket No. FR-5180-P-01

MORTGAGE BANKERS ASSOCIATION
Investing in communities

June 11, 2008

Regulations Division
Office of General Counsel
Department of Housing and Urban Development
451 7th Street, SW
Room 10276
Washington, DC 20410-0001

Re: Comments in Response to the Department of Housing and Urban Development's Real Estate Settlement Procedures Act (RESPA): Proposed Rule to Simplify and Improve the Process of Obtaining Mortgages and Reduce Consumer Settlement Costs, Docket No. FR-5180-P-01

Gentlepersons:

The Mortgage Bankers Association[1] (MBA) appreciates the opportunity to comment on the above-cited proposed rule issued on March 14, 2008 by the United States Department of Housing and Urban Development (HUD) to amend Regulation X, HUD's Real Estate Settlement Procedures Act (RESPA) Regulations.

MBA supports RESPA reform and continues to believe that if done correctly RESPA reform would improve disclosures to consumers concerning their closing costs. As detailed in these comments, however, MBA strongly believes that HUD should work with the Board of Governors of the Federal Reserve System (Board) in a careful, coordinated and comprehensive manner to truly simplify and improve the mortgage process for consumers.

Problems confronting today's mortgage borrowers reveal that while some may have made bad choices, others may have been confused about their credit costs and terms under adjustable rate mortgages and entered into mortgage loans they simply did not understand. Borrowers need clarity about the terms and costs of credit which is the Board's responsibility under the Truth in Lending Act (TILA).

RESPA, which is HUD's responsibility, is intended to provide consumers with disclosures about closing costs. While confusion about closing costs has not been as prominent an issue in the mortgage crisis, borrowers would benefit from greater transparency if the disclosures mandated

[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 370,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,400 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mortgagebankers.org.

under both laws were markedly improved. RESPA and TILA disclosures are to a great extent provided to borrowers at the same time.

The Board has already issued proposed new rules under TILA and the Home Ownership and Equity Protection Act (HOEPA)[2] concerning the mortgage market generally and is expected to soon embark on further reform efforts concerning TILA disclosures specifically; HUD's efforts should be linked to the Board's efforts. Only through concerted and coordinated reform of TILA disclosures regarding the costs of credit, and RESPA disclosures regarding settlement costs, can borrowers be empowered to navigate the mortgage market and protect themselves against abuse.

Specifically, MBA strongly recommends that HUD and the Board work together to produce a combined TILA and Good Faith Estimate (GFE) form and implement it simultaneously to replace the current RESPA and TILA disclosures provided at the time of application. For this purpose, MBA and its members have developed a proposed combined form and a comparable revised HUD-1 attached in Appendix A.

Notwithstanding the significant number of well considered comments it has and will receive advising against it, if HUD moves forward to finalize its proposed GFE and HUD-1 under current law, independent of the Board's reform efforts, MBA urges that it pare back the proposal and accompanying forms to address only closing cost issues. MBA believes HUD's authority is constrained to and within that sphere. MBA would specifically suggest that HUD use the relevant pages of MBA's proposed disclosures displayed in Appendix B to these comments which are confined to RESPA authorized disclosures. MBA believes that, if more comparable GFE and HUD-1 closing cost forms are adopted and used through the mortgage process, and borrowers are enabled to inspect their HUD-1 or HUD-1A the business day before settlement, the proposed closing script can and should be dispensed with entirely. The GFE and HUD-1 disclosures (as proposed in Appendix B) identify mortgage broker fees and reference the mortgage broker fee agreement proposed by the Board and currently required by federal financial regulators.

MBA also recommends that the tolerances be replaced with a *Borrower Protection* approach spelled out later in this letter, utilizing HUD's current authority. The accompanying rule changes to the application process should be dispensed with and instead, GFEs should be provided after application at no or nominal charge, except for the cost of a credit report, unless the borrower determines that he or she wishes a rate lock or to immediately arrange an appraisal. MBA would support HUD proceeding as expeditiously as possible to finalize its proposals concerning average cost pricing and volume discounts, with suggested modifications, as well as making any necessary clarifications regarding electronic disclosures and mortgage servicing transfers. MBA also respectfully requests that HUD address MBA's other comments detailed below.

Finally, MBA would support changes to the current RESPA and TILA statutory framework to complement HUD and the Board's reform effort. MBA will support proposals that carry out the following principles:

[2] 73 Fed. Reg. 1672 (January 9, 2008).

- Disclosures should be streamlined and greatly simplified and uniform throughout the nation; terms that are not consumer friendly should be replaced with terms that are simple and understandable;
- Disclosures should be binding as early in the process as possible, taking into account that during the mortgage process information is developed and circumstances can change;
- The timing of disclosures should not result in undue delay for borrowers to receive needed credit;
- The process should facilitate competition to lower costs as well as the provision of high quality services;
- Borrowers and regulators should be appropriately empowered to prevent abuses;
- Lenders should have a reasonable opportunity to cure errors prior to litigation; and
- Remedies for errors should not result in unduly increased costs for all consumers.

This letter provides background and then sets forth general and specific comments to help achieve HUD's ultimate goal, shared by MBA, of creating a more transparent mortgage process that increases consumer understanding and lowers mortgage costs. MBA also provides responses to questions posed by HUD in the proposal.

I. Background

A. Past Efforts to Reform RESPA

Though the current law was enacted in 1974, as early as the 1980s, the Reagan Administration considered reform of RESPA to simplify the mortgage process. In 1992, HUD amended its RESPA rules to implement amendments to the law to permit affiliated businesses (formerly termed "controlled businesses") in accordance with the requirements of section 8(c)(4).[3] Also in 1992, under an opinion of the HUD Office of General Counsel and then through HUD's 1992 rule revisions, HUD required the disclosure of mortgage broker fees in table-funded transactions.[4]

In 1996, Congress required HUD and the Board to simplify and improve RESPA and the TILA disclosures and, if necessary to make recommendations to Congress to do so.[5] In 1998, as a result, HUD and the Board reported to Congress and made recommendations to establish a firmer GFE and to provide an exemption to RESPA to permit guaranteed packages of mortgage services.[6] About the same time, after considerable litigation and consumer complaints that payments by lenders to mortgage brokers amounted to illegal kickbacks, HUD conducted a negotiated rulemaking and issued a proposed rule concerning the legality and disclosure of mortgage broker fees, which was never finalized.

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[3] 67 Fed. Reg. 49134 (July 29, 2002).

[4] August 14, 1992 legal opinion by Frank Keating, General Counsel, HUD.

[5] See Section 2101 of the Economic Growth and Regulatory Paperwork Reduction Act of 1996, Pub. L. No. 104-208, 110 Stat. 3009.

[6] Joint Report to Congress Reform to the Truth in Lending Act and Real Estate Settlement Procedures Act, Board of Governors of the Federal Reserve System, Department of Housing and Urban Development (July 1998).

In 1999 and 2001, in the face of continuing litigation concerning the legality of mortgage broker fees, HUD issued policy statements clarifying its position on the issue that also included a call for improved disclosure.[7] Industry groups supported the policy statement.

In 2002, nearly six years ago, HUD proposed to reform its disclosure requirements under RESPA to: (1) establish an exemption from Section 8 of RESPA for guaranteed mortgage packages; (2) revise its good faith estimate requirements to establish tolerances for those not seeking the mortgage package exemption; and (3) improve the disclosure of mortgage broker fees. As a result of opposition to the rule from the title, mortgage brokerage and ultimately the mortgage lending and real estate brokerage industries, HUD withdrew its proposal in 2004.

In 2005, HUD sponsored seven roundtables to solicit the views of industry and consumer groups, including small businesses, regarding RESPA reform.

B. Rulemaking versus Legislative Solutions

In 1996, Congress directed the Board and HUD to simplify and improve their mortgage disclosures through rulemaking where possible. If legislative changes were required, the Board and HUD were to make recommendations to Congress. In 1998, the Board and HUD concluded that "meaningful change could come only through legislation."[8] In 2002, however, and in this 2008 rulemaking, HUD determined that it had sufficient authority under RESPA to simplify and improve RESPA disclosures.

In this comment letter, MBA addresses HUD's current regulatory proposals and urges its linkage with anticipated regulatory action by the Board. MBA believes, however, that HUD's authority is limited under current law and responds to these proposals in that vein. As indicated, MBA would support complementary statutory changes that truly simplify and improve the mortgage process consistent with the above principles including, for example, revisions to facilitate early firm disclosures and changes to TILA to change the statute's required disclosures to make them much more relevant and usable.

C. The Current RESPA Proposal

The proposed rule would: (1) establish a four-page standard Good Faith Estimate (GFE) form; (2) impose tolerances to limit increases in GFE estimates at closing; (3) revise requirements for disclosure of mortgage broker fees as 'the charge or credit for the interest rate chosen;" (4) make changes to the HUD-1 to facilitate comparison between GFE and HUD-1 charges; (5) establish a new script to be read to borrowers at settlement concerning final loan terms and settlement costs; (6) revise regulations to permit certain average-cost pricing and volume discounts; (7) clarify "required use" requirements to restrict disincentives to use of non-affiliates; and (8) make technical amendments to the RESPA rules. The proposal also announces that HUD will seek legislative proposals to increase enforcement authority, including injunctive authority, under RESPA concerning the GFE and HUD-1, servicing, Section 8, title insurance

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[7] *See* RESPA Statement of Policy 1999-1, 64 Fed. Reg. 10080 (March 1, 1999), and Clarification of RESPA Policy Statement 1999-1, 66 Fed. Reg. 53052 (October 18, 2001).
[8] Joint Report to Congress Concerning Reform to the Truth in Lending Act and the Real Estate Settlement Procedures Act, p. 2, Board of Governors of the Federal Reserve System, Department of Housing and Urban Development (July 1998).

and escrow accounts. The proposal currently would invite public comment for 60 days from the date of Federal Register publication.

In this proposal, HUD has also announced that it intends to seek legislative changes to: (1) authorize the Secretary to impose civil money penalties for violations of Section 4 of RESPA (the Settlement Statement), Section 5 (the GFE and Special Information Booklet), Section 6 (servicing), Section 8 (kickbacks, referral fees and unearned fees), Section 9 (title insurance), and Section 10 (escrows); (2) require delivery of the HUD-1 to the borrower three days prior to closing; and (3) expand and make uniform the statute of limitations applicable to governmental and private actions under RESPA.

A more detailed summary of the statute and the regulatory proposal is contained in Appendix E.

II. MBA's Comments

A. Overview - MBA's VIEWS ON THE RESPA PROPOSED RULE

Since HUD last issued its proposed rule in 2002,[9] the real estate industry and the mortgage system have experienced a crisis of a magnitude that was largely unexpected and has been nearly unprecedented. While the crisis has resulted in pervasive dislocation and hardship for consumers and businesses alike, its benefit has been to again bring into focus what has been working in the mortgage system and what must be improved.

This crisis has many victims and causes. The causes range from economic conditions, excess capacity and escalating real estate prices to outsized investor and borrower appetites. The victims include more than borrowers themselves but also include future borrowers, communities and the economy at large.

While MBA does not believe that the lack of transparency in the mortgage process is the main cause of borrower difficulties, or that its improvement is the only solution, greater transparency could help stem abuses. The sheer volume and opacity of disclosures today allows abusers to hide in plain sight. Long before the current market crisis, MBA consistently supported and invested considerable resources in mortgage simplification and much greater financial literacy for consumers in the mortgage market. MBA now believes that problems in the industry are a good reason to redouble efforts in both these areas.

Greater transparency would better empower consumers to understand and pick among the range of choices available from the mortgage market based on their own financing needs and risk appetites while at the same time allowing them to shop and compare offers.

MBA applauds HUD's continuing efforts at improving RESPA disclosures. At the same time, MBA also applauds the Board's recent efforts to improve mortgage broker fee disclosures[10] and

[9] 67 Fed. Reg. 49134 (July 29, 2002).
[10] 73 Fed. Reg. 1672 (January 9, 2008).

underwriting under its recent HOEPA rule[11] as well as its recognition that TILA disclosures need updating to reflect the increased complexity of mortgage products.[12]

As recent events demonstrate, borrowers need greater clarity about the terms and costs of credit which is the Board's responsibility under the Truth in Lending Act (TILA). RESPA, which is HUD's responsibility is intended to provide consumers with disclosures about closing costs and should accompany TILA reform. RESPA and TILA disclosures are ordinarily provided to borrowers at the same time.

Problems confronting today's mortgage borrowers reveal that while some may have made bad choices, others may have been confused about their credit costs and terms under adjustable rate mortgages and entered into mortgage loans they simply did not understand. Confusion about closing costs and related issues, except for concerns about steering which implicate both laws, has not been a prominent issue in the mortgage crisis. To improve consumer understanding of both the terms and costs of credit and closing costs, HUD and the Board must work together in the reform process to make both RESPA and TILA disclosures clearer and more compatible.

While these efforts are needed, HUD's efforts come at a time of retrenchment in the industry and a credit crunch for borrowers. To minimize costs to the industry and borrowers, changes must be undertaken judiciously and in combination. New disclosure requirements that necessitate new systems changes, training and staffing will be extremely costly and could not come at a more difficult time.

Having evaluated HUD's current proposal, and the Board's new proposal concerning disclosures thus far in the HOEPA rule, it is clear that there are considerable variations between the Board and HUD's approaches to reform. Mortgage broker fee disclosure is an excellent example. The Board proposes a clear agreement between broker and consumer while HUD's approach is far from direct. Also, HUD's proposed summary of loan terms discloses many of the terms of credit which are the Board's province under TILA but, at the same time, discloses only the note rate of the loan and not the annual percentage rate (APR) as it appears on the TILA disclosure today. This anomaly will prove confusing to both consumers and industry.

MBA's Overarching Comment

Considering the costs of changes including system conversions necessary to accommodate new requirements and, most importantly, the need for borrowers to better understand both the terms of their loans as well as their costs, MBA strongly believes that HUD's efforts should not be finalized until they are combined and harmonized with the Board's efforts to reform its TILA disclosures. HUD and the Board should work together to develop, reissue and finalize joint rules to simplify both the RESPA and TILA disclosures. Toward this end, MBA is furnishing, as Appendix A of this comment letter, a suggested joint RESPA-TILA disclosure.

[11] 73 Fed. Reg. 1672 (January 9, 2008).

[12] "The Board recognizes that [TILA] disclosures need to be updated to reflect the increased complexity of mortgage products. In early 2008, the Board will begin testing current TILA mortgage disclosures and potential revisions to these disclosures through one-on-one interviews with consumers. The Board expects that this testing will identify potential improvements for the Board to propose for public comment in a separate rulemaking." 73 Fed. Reg. 1673 (January 9, 2008).

MBA believes that only through comprehensive reform can consumers take advantage of better transparency and lower costs. MBA requests that both HUD and the Board involve industry and consumer advocates to help shape the proposals and that it utilize consumer testing to ensure that improvements do in fact increase consumer understanding. Separate and conflicting efforts will create more confusion for consumers and increase costs for everyone involved.

If, notwithstanding the requests from this industry and others, HUD determines to go forward and finalize the proposed RESPA rule independently, MBA believes the effort should be pared back considerably and put on a timeline that would match the Board's forthcoming disclosure reform efforts under TILA. In case HUD goes forward with the rulemaking, MBA submits the following comments, as detailed in this letter:

1. **HUD's summary of loan terms should be excluded from the GFE and should be issued by the Board in consultation with HUD;**

2. **MBA has particular concerns about key definitions in the proposal including the proposed definitions of "mortgage broker" and "originator," which should be revised;**

3. **MBA supports improvement of the GFE and HUD-1 and harmonization between the forms, it therefore has strong concerns about HUD's overall disclosure approach;**

4. **MBA believes HUD's proposed GFE would overload the borrower with material, counter to HUD's and MBA's goal of ensuring that the consumer focuses on important information regarding mortgage costs. MBA urges HUD to work with the Board to finalize a combined RESPA-TILA form or, if it proceeds independently, to finalize a GFE form as proposed by MBA in the attached Appendix B;**

5. **MBA supports revision of the GFE to separately disclose mortgage broker charges and complement the Board's proposed mortgage broker fee agreement;**

6. **While MBA appreciates HUD's efforts to facilitate shopping, this aspect of the rule should not be finalized because of the difficulties of coordinating the concept with other laws. An alternative approach should be adopted;**

7. **While MBA supports methods to stem increases in fees from lenders and mortgage brokers from the time of application until settlement, it has serious concerns about HUD's proposal to limit lenders to a "zero tolerance" and to make them responsible for the charges of third-party providers. It believes retention of the "good faith" standard is consistent with the statute and that a bright line Borrower Protection approach should be established to help protect borrowers from fee increases;**

8. **The proposed changes to the HUD-1 to refer to the new GFE fail to achieve the objective of making the GFE and HUD-1 harmonious and readily comparable;**

9. **HUD should not Implement a "closing script" to be read at closing and to be signed by the borrower;**

10. **MBA supports, with some modifications, HUD's proposal to clarify that lenders and brokers can use average cost pricing for settlement services within any class of transactions;**

11. **While MBA supports HUD's proposal to clarify the legality of volume discounts, MBA believes the proposal is too restrictive;**

12. **Concerning the proposed revisions to prohibitions against requiring the use of affiliates, MBA believes it would be sufficient for HUD to reaffirm that it may scrutinize discounts to ensure that they are *bona fide* rather than enact rules that would risk depriving borrowers of certain discounts altogether;**

13. **MBA generally supports HUD's efforts to update its RESPA regulations concerning mortgage servicing transfers and escrows and to explicitly recognize the applicability of ESIGN[13] to RESPA;**

14. **MBA will evaluate HUD's legislative proposals as they are developed in accordance with key principles to ensure transparency and facilitate the mortgage market; and**

15. **MBA supports an implementation schedule that would link implementation of this rule to the Board's forthcoming TILA reform rule.**

B. HUD and the Board Should Coordinate on Comprehensive RESPA-TILA Reform

As indicated, MBA strongly supports simplification of the mortgage process. Nevertheless, HUD's proposal should not be finalized at this time; rather HUD should work in concert with the Board's efforts to reform TILA so that reform of mortgage disclosure best serves consumers.

RESPA and TILA are the primary laws Congress enacted to require certain mortgage information be provided to consumers.[14] They cover different aspects of the same transaction. As indicated, RESPA is intended to provide consumers information on their closing costs and TILA is intended to provide consumers information on the terms and costs of credit. RESPA and TILA disclosures are provided to most borrowers at the same time during the mortgage process.

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[13] On June 30, 2000, Congress enacted the ESIGN Act (15 U.S.C. §7001-7031) to facilitate the use of electronic records and signatures in interstate and foreign commerce by ensuring the validity and legal effect of contracts entered into electronically. Careful to preserve the underlying consumer protection laws governing consumers' rights to receive certain information in writing, Congress imposed special requirements on businesses that want to use electronic records or signatures in consumer transactions. Section 101(c)(1)(C)(ii) of the Act requires businesses to obtain from consumers electronic consent or confirmation to receive information electronically that a law requires to be in writing. The Act went into effect in October 2000.

[14] The Truth in Lending Act covers credit in addition to mortgages: "It is the purpose of this subchapter to assure a meaningful disclosure of credit terms available to him and avoid the uninformed use of credit, and to protect the consumer against inaccurate and unfair credit billing and credit card practices" (TILA §102, 15 U.S.C. §1601).

Problems in the mortgage market indicate that while some borrowers may have made bad choices, the difficulties of others, in part, may have involved confusion concerning the terms of their mortgages rather than merely the costs for them.[15] Others may have entered into products they did not understand. Better information on both credit terms and loan costs, as well as better information on mortgage broker compensation, would greatly empower borrowers and protect them from abuse. The need for improvements in both understanding credit and settlement costs strongly militates in favor of both HUD and the Board working together in the reform process so that both RESPA and TILA disclosures are compatible.

Piecemeal, sequential or *seriatim* reform of the RESPA disclosures, on the other hand, followed by reform of the TILA disclosures, would be extremely costly to businesses both small and large, and ultimately to consumers. New disclosures along the lines HUD proposed will require substantial retooling of systems and considerable expenses for training, compliance and staffing. Changes to TILA are expected to result in similar costs. Since the mortgage crisis has led to tightened and more costly credit for lenders and borrowers alike, these very considerable expenses would occur at just the time that the industry and consumers can least afford them. Moreover, if the efforts of the agencies are not compatible they will greatly confuse consumers and increase the costs to industry and consumers even more.

HUD's own Regulatory Flexibility Analysis estimates that the total one-time costs to the lending and settlement industries of the new GFE and HUD-1 alone will be $570 million, $390 million of which are estimated to be borne by small business.[16] HUD estimates that the total recurring costs are estimated to be $1.231 billion annually or $98.74 per loan. While MBA believes these costs are underestimates, even if they were accurate, the costs of TILA reform, following after these costs are incurred, can be expected to result in costs of similar size for retooling, retraining, re-staffing and other costs to the industry.[17] If, on the other hand, RESPA and TILA changes were accomplished together, it is reasonable to anticipate that economies could result in lower costs for both RESPA and TILA reforms if performed simultaneously.

In any event, hasty efforts at mortgage reform should not be justified based on current market difficulties. While it is clear that borrowers are experiencing higher default and foreclosure rates today than they have in recent years, the great majority of loans and borrowers in the nonprime market are performing well, as are the vast majority of prime loans. The area of greatest concern has been nonprime adjustable rate mortgage (ARM) loans and particularly hybrid ARMs (which employ an extended introductory rate period with an adjustable rate feature at the end of the introductory period) which are generally no longer available in today's market to these borrowers. While there are concerns that steering by mortgage brokers may have been part of the problem, there is no apparent evidence that closing costs have been a major aspect of it.[18]

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[15] MBA data of the third quarter of 2007 showed significant percentages of investor properties among all loan types in several states: Arizona 22 percent; California 16 percent; Florida 22 percent; and Nevada 22 percent.
[16] 73 Fed. Reg. 14102 (March 14, 2008).
[17] Schnare, Ann B., The Estimated Costs of HUD's Proposed RESPA Regulations, National Association of Realtors, (June 3, 2008).
[18] See 73 Fed. Reg. 1698-1700 (January 9, 2007).

It must also be borne in mind that as mortgage applications have risen over the last two decades, so too have the percentage of families realizing – and successfully sustaining – the dream of homeownership. This is due to several main factors including lower interest rates (which are at historically low levels – even today), risk-based pricing and a host of industry efforts and innovations. According to the Board's Flow of Funds data,[19] the value of residential real estate assets owned by households has increased from $10.4 trillion in 1999 to $20.1 trillion as of the first quarter of 2007, and aggregate homeowner's equity now is $9.6 trillion. Unnecessarily increased costs that might stem from unwise reforms should not be allowed to undermine the objective of sustainable homeownership.

C. If HUD Goes Forward Independently

Once again, MBA strongly reiterates that HUD and the Board must work together in the interests of industry and consumer alike. However, if HUD decides to finalize the proposed rule without such coordination, MBA believes the rule should be pared down and several significant changes should be made before a final rule is published.

1. HUD's summary of loan terms should be excluded from the GFE and should be issued by the Board in consultation with HUD.

MBA strongly believes that while a "Summary of Your Loan Terms" could be very useful to provide borrowers with key information to better understand mortgages and to shop among them, it should not be part of the HUD proposal and should be developed and issued by the Board. Were HUD and the Board to separately issue such summaries, the efforts would be duplicative and confusing.

While HUD's proposed summary includes "adjusted origination charges", "charges for other settlement services" and "total estimated settlement charges" (discussed below), it mostly includes points relevant to credit costs and terms. These include: "Your initial loan balance;" "Your initial monthly payment owed for principal, interest and any mortgage insurance is;" Your rate lock period is;" "Can your interest rate rise?;" "Can your loan balance rise?;" "Can your monthly payment amount owed for principal interest and any mortgage insurance rise?;" "Does your loan have a prepayment penalty?;" Does your loan have a balloon payment;" and "Does you loan include a monthly escrow payment for property taxes and, possibly, other obligations?" Considering that these are matters relevant to credit costs which are the Board's responsibility under TILA, this type of disclosure should be issued by the Board in consultation with HUD.

While HUD's proposed summary displays the "initial interest rate," it does not include the "annual percentage rate" or "APR" or the Finance Charge" and the "Amount Financed." Although MBA believes these terms themselves cause confusion, the Truth in Lending Act requires their use at this time. Pending amendments to delete them, which MBA would support, a summary that does not address them will likely cause confusion if they are still disclosed under TILA. Also, by dealing with the matters of "balloon payments" and "prepayment penalties," the summary is unnecessarily repetitious of the TILA disclosure. The Board also

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[19] The Board's Flow of Funds data may be viewed at the following Website: http://www.federalreserve.gov/releases/z1/current/default.htm.

should issue the summary to assure its consistency with forthcoming TILA disclosures as well as current ones.

MBA believes the Board, in arriving at a summary form, should utilize the input of concerned groups as well as consumer testing. In that process, as well as in the process of combining RESPA and TILA forms, the goal should be to lessen the amount of paper that consumers confront to navigate the settlement process. Considering that closing costs may appear in the summary, the Board should consult with HUD on this matter going forward.

2. Definitions – MBA has particular concerns about key definitions in the proposal including the proposed definitions of "mortgage broker" and "originator," which should be revised.

HUD would change the definition of mortgage broker to mean a "person (not an employee of the lender) or entity that renders origination services in a table funded or intermediary transaction." The definition would also apply to a loan correspondent approved under 24 C.F.R. § 202.8 for Federal Housing Administration (FHA) programs. This formulation would include an "exclusive agent" under the definition of "mortgage broker."

MBA, however, does not believe the definition should be changed to include exclusive agents of lenders and it also does not believe that that the term "intermediary" should be injected into the definition at all. MBA believes that mortgage lenders, including their agents and employees, are functionally different from mortgage brokers, and should therefore be treated differently by law. To clarify this and other related issues, MBA has recently published the attached paper "*Mortgage Bankers and Mortgage Brokers: Distinct Businesses Warranting Distinct Regulation*" which is attached as Appendix D to these comments.[20]

The paper points out that mortgage brokers are middlemen that facilitate or make arrangements for loans and that lenders, on the other hand, lend money. Consumers perceive brokers and lenders differently. Consumers regard mortgage brokers as shopping for them and ordinarily cease their own shopping when they deal with them, ceding the shopping to the broker. In contrast, consumers regard lenders (and their employees and agents) as providers of loan products amongst whom they shop and compare.

Because mortgage brokers are regarded as shopping for borrowers, they present a greater potential risk of steering consumers. Accordingly, MBA believes it is appropriate for brokers, for example, to disclose that they receive additional compensation from lenders. MBA does not believe that lenders or their exclusive agents warrant the same treatment because borrowers do not perceive them the same and they do not present the same risks.

Further, MBA does not believe the term "intermediary" should be injected into the definition at all, unless it is defined to clearly cover independent mortgage brokers. As it stands, the term is undefined and could be misinterpreted to cover some loan officers who work for lenders and may be independent contractors.

[20] The paper is also available on the Web at the following address: http://www.mortgagelenders.org/files/News/InternalResource/62646_Paper.pdf.

The proposed rule would also define "loan originator" as meaning a "lender or mortgage broker." It also would introduce the term into several definitions including "closing script," "good faith estimate application," "mortgage application" to name a few. MBA believes, however, that since a "lender" and "mortgage broker" are different they, should not be defined with a single term. MBA believes that borrowers do understand the differences between "mortgage lenders" and "mortgage brokers" and urges that HUD not blur these differences and create confusion for borrowers.

While MBA understands that some advocates for the mortgage brokerage industry argue that a "level playing field" requires this blurring, the fact is that the players and their functions are substantively different. As described more fully below, these efforts blur these distinctions and obfuscate the differing regulatory needs of consumers regarding lenders and brokers. [21]

3. MBA supports improvement of the GFE and HUD-1 and harmonization between the forms, it therefore has strong concerns about HUD's overall disclosure approach.

MBA believes as a general matter that the proposed GFE is far too long and will be largely ignored by consumers. While it appreciates that the first page is intended to be a summary, and the second page a list of closing costs, MBA strongly believes, as discussed below, that no matter how laudable the educational purposes of the rest of the form may be, the form's sheer length will cause borrowers to ignore its important information.

The proposed changes to the HUD-1, while appreciated, also fall short of making the GFE and HUD-1 correspond, necessitating the use of a "closing script" to be read by the closing agent and signed by the borrower. The GFE is visually different from the HUD-1. While the HUD-1 has been somewhat rearranged it mainly only refers to lines on the GFE. MBA believes that a better approach would be to make the GFE more closely correspond to the HUD-1, so that the consumer could easily compare the two documents, eliminating the need for the closing script altogether. The forms in Appendix B more closely correspond and should be adopted by HUD if it moves forward independently.

4. MBA believes HUD's proposed GFE would overload the borrower with material, counter to HUD's and MBA's goal of ensuring that the consumer focuses on important information regarding mortgage costs. MBA urges HUD to work with the Board to finalize a combined RESPA-TILA form or, if it proceeds independently, to finalize a GFE form along the lines of the attached Appendix B.

HUD and the Board Should Issue a Combined GFE-TILA Disclosure

As indicated, MBA strongly supports a combined and coordinated effort by HUD and the Federal Reserve to develop and implement a joint GFE-TILA disclosure. For this purpose, industry representatives – including MBA members – have developed the attached two-page form at Appendix A with the first page displaying the settlement costs and the second page displaying the costs of credit for a consumer's mortgage.

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[21] A comment letter transmitted on June 4, 2008, from the Federal Deposit Insurance Corporation to HUD in regards to the proposed rule objects to this provision of the proposal because it blurs the distinction between brokers and bankers.

If, however, HUD goes forward to finalize the GFE independently, MBA recommends that HUD use the form as modified and set forth in Appendix B and implement the rule on the same schedule as the Board's changes under TILA. MBA provided an earlier version of the form to HUD which HUD critiqued in its Regulatory Flexibility Analysis.[22] This version has been revised to address these comments and is discussed below. Before discussing the MBA form, MBA offers the following comments on HUD's proposed GFE and HUD-1.

HUD's Proposed GFE

HUD's proposal would establish a standard four-page GFE form.[23] The form would:

(1) Disclose, in a summary, the loan details specifying the loan amount, term, interest rate, initial payment, rate lock period, whether the amounts for principal, interest and mortgage insurance can rise, whether the loan has a prepayment penalty or a balloon payment and whether the loan includes a monthly escrow payment for taxes and insurance; as well as "adjusted origination charges", "charges for other settlement services" and "total estimated settlement charges."

(2) Disclose the costs in ten cost categories including:

(a) Lender and mortgage broker charges known as "our service charge;
(b) The YSP or points as "credit or charge for the interest rate chosen," and then "adjusted origination charges;"
(c) Required services selected by the originator;
(d) Title services and title insurance;
(e) Required services the borrower can shop for;
(f) Government recording and transfer charges;
(g) Reserves or escrow;
(h) Daily interest charges;
(i) Homeowner's insurance; and
(j) Optional owner's title insurance;

(3) Advise the borrower of the relationship between the interest rate and the borrower's settlement costs; and

(4) Disclose various other information for borrowers including how to apply for the loan, estimated taxes, flood and property insurance premium information, a shopping chart, and information about lenders receiving additional fees by selling the loan at a future date.

While MBA appreciates HUD's effort to create a comprehensive document to help the borrower shop and better understand the mortgage process, MBA believes the resultant document is far

[22] Pages 4-8 through 4-11 and 4-19 through 4-20, Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis, FR-5180-P-01, Proposed Rule to Improve the Process of Obtaining Mortgages and Reduce Consumer Costs, Department of Housing and Urban Development (March 2008).
[23] See proposed GFE form at 73 Fed. Reg. 14095-8.

too long and would overload the borrower with material that ultimately would be ignored and therefore counterproductive to HUD's and MBA's own consumer protection objectives.[24]

As indicated, RESPA requires that lenders provide a "good faith estimate" of the amount or range of charges for specific settlement services the borrower is likely to incur in connection with the settlement as developed by the Secretary in conjunction with a Special Information Booklet prescribed by HUD.[25]

MBA's Comments on HUD's Form

While MBA generally supports the grouping of the amount or ranges of specific services on the GFE in a manner that is comprehensible and comparable, the form itself should be modified so it is mainly a list of charges with minimal supplementary material, as is the MBA form in Appendix B. MBA believes most of the material on the form, except the costs, should be moved to explanatory materials, such as the Special Information Booklet.

MBA's specific comments regarding the proposed GFE are as follows:

(1) The term "originator" and "origination" services should not be used on the form. Instead the terms "lender" and "mortgage broker" should be used. As indicated, the latter terms are understood by many borrowers and using another term will only obfuscate the different functions of brokers and lenders.

(2) Unless a combined RESPA-TILA form is issued in conjunction with the Board, the Instructions portion should indicate that the GFE simply gives an "estimate of settlement charges" rather than "settlement charges" and "loan terms."

(3) Accompanying instructions should fully explain the rules governing GFE estimates including that costs may increase for a variety of valid reasons. If the point concerning when the loan must be closed is included on the form, it should note that the date will not finally be set until the borrower actually applies for a loan and that such date may be governed by the rate lock chosen by the lender and borrower.

(4) The information concerning how long the costs and interest rate are open to borrower acceptance needs greater clarification and could be provided in accompanying materials. Borrowers should be informed that they are not required to lock the rate on the GFE and they may lock in a different rate at a different cost at a different time. If this material is included in the GFE form, the accompanying rule instructions also should make clear that the interest rate in the GFE may be available until a specified hour and date. Rates frequently change several times a day.

(5) While MBA believes that a "Summary of Your Loan Terms" could be useful, the summary should be removed from the GFE and issued by the Board in consultation with HUD.

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[24] A comment letter transmitted on June 4, 2008 to HUD from the Federal Deposit Insurance Corporation indicates that in light of its own testing of consumers it has the same concern.

[25] The "good faith estimate" and the booklet are authorized under Section 5 of RESPA (12 U.S.C. §2604).

(6) The use of the term "Adjusted Origination Charge" at the bottom of the first page is not at all helpful to consumers. It introduces new terminology in a setting where it is already difficult for the consumer to understand the costs themselves.

(7) Similarly, on the top of the second page, MBA does not regard the introduction of the new term "Our service charge" to cover both lender and broker fees as helpful to the lending industry or illuminating to consumers.

(8) All of the materials on page three, advising on how to shop and which charges can change at settlement should be moved to explanatory materials. It simply takes up too much space and lengthens the form.

(9) The material on "looking at tradeoffs" also should be moved to explanatory materials, possibly a Shopping Tool to be developed in conjunction with the Board. (An example of a Shopping Tool is attached as Appendix C.) While MBA supports the concept of providing borrowers with hypothetical information on loan alternatives, and does so through its Home Loan Learning Center, homeloanlearningcenter.com, it does not support the idea of requiring lenders to provide alternative mortgage information on the GFE. Also, the information proposed by HUD to be provided involves comparative interest rates and monthly payments involving loan terms. This type of information, if provided at all, should be provided by the Board under TILA.

(10) Similarly, all of the information on page four, with the possible exception of "how to accept the GFE", should be moved to the accompanying materials. A description of the homeowner's financial responsibilities, how they should get more information, and how to use a shopping chart, while well-intended, needlessly lengthens the form and risk its disregard by the borrower.

(11) Finally, MBA does not believe the material on whether lenders can receive additional fees by selling the borrower's loan after settlement is helpful to borrowers. Because the text does not concern settlement or settlement costs, MBA believes it is outside the purview of RESPA.

MBA's Proposed Form

Two years ago, MBA developed with its members, and provided to HUD its own proposed GFE form. In HUD's Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis, HUD critiqued the form.[26] In its analysis, HUD objected to the presentation of the yield spread premium (YSP) and supported its own approach. HUD said that the distinction between mortgage lenders and mortgage brokers on MBA's form would create confusion because consumers, it believes, are unfamiliar with the meaning of these terms. HUD criticized the print size on the form pointing out that explanations were one size smaller than the material disclosed and HUD was also concerned about the form's readability if it was sent via facsimile. The

[26]Pages 4-8 through 4-11 and 4-19 through 4-20, Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis: Proposed Rule to Improve the Process of Obtaining Mortgages and Reduce Consumer Costs (March 14, 2008).

analysis also expressed concern about the presentation of certain components of a monthly mortgage payment, mainly the mortgage insurance payment. Finally, HUD expressed concern that MBA's grouping of fees was arbitrary, e.g., valuation included both credit reports and appraisals.

HUD also provided comments on MBA's proposed HUD-1 in its analysis. HUD objected to the omission of a place for charges paid outside of closing. HUD pointed out that the "actual monthly payment" in MBA's HUD-1 is different from the "estimated monthly payment" which will cause confusion. It also indicated that the direction to compare the HUD-1 and GFE charges are wrong in suggesting that only the borrower's charges are to be compared; borrower and seller payments should be compared. HUD also expressed other concerns about some of the category groupings, the absence of any label on line 704 and line 850 is missing a place for the borrower payment.

MBA has revised the forms, which are now the first pages of the combined RESPA-TILA forms at Appendix A, and displayed as separate RESPA forms at Appendix B, to address most of HUD's concerns. MBA maintains, however, that consumers should be made aware with great clarity of the respective fees of lenders on the one hand and mortgage brokers on the other. Consumers should be made aware of the differences between lenders and brokers and HUD should not increase borrower confusion. MBA has changed its broker disclosure so that the broker fee reflects total compensation to the mortgage broker and the lender's payment on the borrower's behalf. It has also revised the form to reference the mortgage broker fee agreement that the Board has proposed and other regulators are requiring. Notably, Office of the Comptroller of the Currency (OCC) examiners have been requiring disclosures along these lines by federally regulated institutions since April 1, 2008 pursuant to the OCC's Advisory Letter 2003-3.

Rather than provide notations on the form concerning "payments outside of closing" which are not well understood by borrowers, the GFE and the HUD-1 at Appendix B provides a disclosure at line 1701 of "Amounts Paid by Borrower Before Closing."

The recommended form is much shorter and was developed by those who make mortgage loans and day-in and day-out are presented with consumer questions. It is also readily comparable to the revised HUD-1, also at Appendix B and also developed by MBA and presented to HUD. MBA believes the use of these comparable forms throughout the mortgage process at shopping, at or following application, following underwriting and at and a day before closing would eliminate the need for the closing script and reduce costs to small and large businesses.

HUD's own Regulatory Flexibility Analysis estimates that the total one-time costs to the lending and settlement industry of the new GFE and HUD-1 alone will be $570 million, $390 million of which are estimated to be borne by small business.[27] HUD estimates that the total recurring costs are estimated to be $1.231 billion annually, or $98.74 per loan. While MBA believes that there will be retooling costs associated with implementation of its shorter GFE and HUD-1, it believes that its forms cover less ground and will be easier for borrowers to understand, resulting in fewer questions and concerns directed to industry. MBA believes these differences

[27] 73 Fed. Reg. 14102 (March 14, 2008).

will translate into lower initial – and much lower recurring – costs for businesses large and small, as well as for borrowers.

Again, MBA maintains that the form in Appendix B is much more useful than HUD's proposed GFE. While HUD indicates at length that it tested its proposed form, MBA has profound concerns about the nature and scope of the testing. MBA believes that, in an atmosphere where borrowers are literally inundated with paper during the mortgage process, effective testing should also include a consideration whether the many additional pages proposed by HUD enhance or actually detract from the consumer's ability to understand the costs and terms of their mortgage. MBA believes that in the context of combined RESPA-TILA or, if HUD goes forward independently, much more comprehensive testing is required.

5. MBA supports revision of the GFE to separately disclose mortgage broker charges and complement the Board's proposed mortgage broker fee agreement.

Board Proposal and Federal Financial Regulator Requirements

MBA has long supported the straight-forward disclosure of mortgage broker fees in a manner similar to that proposed by the Board in its HOEPA proposal[28] as the best way to protect consumers and finally resolve this issue which has bedeviled industry and consumers for years. Recently, legislators have sought to limit or eliminate yield spread premiums (YSPs). While MBA strongly supports the legality of YSPs and other fees paid by lenders to help defray borrowers' closing costs, MBA believes that to assure that they do not simply augment costs, unbeknownst to consumers, and to avoid the unwitting steering of consumers by mortgage brokers to higher rate products, consumers must be clearly advised of payments made to mortgage brokers by lenders based on the interest rate. MBA strongly believes that the new GFE, therefore, should include provisions making it compatible with the mortgage broker fee agreement the Board has proposed, and similar agreements required by federal regulators.

HUD's proposed GFE and HUD-1 makes no such provision. Instead it would revise the requirement for disclosure of YSPs from lenders to mortgage brokers as "a charge or credit for the interest rate chosen." This amount would be subtracted from the lender and brokers' "service charge" to arrive at the "adjusted origination charge." The costs occasioned by the adoption of a new terminology for mortgage broker fees will be enormous but its benefits are not apparent.

While MBA appreciates HUD's efforts to clarify the function of a YSP in relation to the interest rate, MBA believes that this could be accomplished without creating confusing new terminology for broker fees. HUD's approach to mortgage broker disclosures, in MBA's view, would be unclear to borrowers. In fact, it further confuses the issue by disclosing discount points as charges in the same block as YSPs. Also, it is possible in the future that some brokers will be paid on a basis other than a loan's interest rate and HUD form does not encompass that possibility.[29]

[28] 73 Fed. Reg. 1672 (January 9, 2008).

[29] The Board proposed that if a broker is compensated on a basis other than an interest rate, it may not have to enter into the agreement with the borrower. The proposal would "provide creditors two alternative ways to comply, one where the creditor complies with a state law that provides consumers equivalent protection, a second where a

The GFE at Appendix A, on the other hand, discloses to the borrower in plain English the total compensation for the broker's services and the amounts paid by the lender to the broker on the borrower's behalf. It also makes clear that the amounts paid to the broker by the lender are paid by the borrower through the loan's interest rate and monthly payment as follows:

> ***Important Information When Using a Mortgage Broker.*** *If you have agreed that the Lender may pay the Broker on your behalf part of the Total Broker Compensation (line 902), you will pay this amount through your loan's interest rate and monthly payment. Your Mortgage Broker is required to enter into a Mortgage Broker Fee Agreement with you which you should review.*

Based on the preamble, the proposed rule and the Regulatory Impact Analysis,[30] MBA understands that HUD's approach to disclosure is shaped by concerns from mortgage brokerage industry advocates and the Federal Trade Commission (FTC) that the form should provide a "level playing field" between brokers and lenders. MBA believes that these assertions are incorrectly premised and typify confusion about brokers' and lenders' respective functions. They do not appropriately consider the risks of steering. Moreover, HUD's approach to disclosure is not shared by other regulators.[31]

As indicated, lenders and brokers perform distinct functions in the marketplace and are perceived differently by consumers. As explained in the attached paper at Appendix D, they are not the same players; they do not have the same role, and applying the same rules to them is ill-advised.

Specifically, considering that consumers regard brokers as middlemen who comparison shop for them, it is wholly appropriate for the consumer to know if the broker is also receiving a fee from the lender based on the consumer's choice of a higher rate. Armed with compensation information, and other information on the relationship between the interest rate and settlement costs, the consumer can make an informed choice and avoid steering and abuse.

Requiring separate disclosures of mortgage lender fees and mortgage broker compensation is also far more consistent with HUD's approach that mortgage brokers provide settlement

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creditor can demonstrate that its payments to a mortgage broker are not determined by reference to the transaction's interest rate. The first safe harbor is for a creditor payment to a broker for a transaction in connection with a state statute or regulation that (a) expressly prohibits the broker from being compensated in a manner that would influence a broker to offer loan products or terms not in the consumer's interest or not the most favorable the consumer could obtain; and (b) requires that a mortgage broker provide consumers with a written agreement that includes a description of the mortgage broker's role in the transaction and the broker's relationship to the consumer, as defined by such statute or regulation. An example would be a state statute or regulation that imposed a fiduciary obligation on a mortgage broker not to puts its own interests ahead of the consumer's and required the broker to disclose this obligation in an agreement with the consumer. ¶The second alternative is for a creditor that can demonstrate that the compensation it pays to a mortgage broker in connection with a transaction is not determined, in whole or in part, by reference to the transaction's interest rate. For instance, if a creditor can show that it pays brokers the same flat fee for all transactions regardless of the interest rate, the creditor would not be subject to the restriction on payments to brokers under § 226.36(a)(1)." 73 Fed. Reg. 1700 (January 9, 2008).

[30] *See* 73 Fed. Reg. 14030 (March 14, 2008).

[31] Both the Board and the FDIC have supported different approaches as shown in the HOEPA proposed rule and the comment letter on this proposal from the FDIC.

services distinct from lenders. HUD's own Statements of Policy issued in 1999 and 2001[32] indicated that mortgage brokers provide distinct goods, facilities or services and to justify such compensation, mortgage broker compensation must be reasonably related to the value of such goods, facilities and services. The Statements directed separate disclosure of mortgage broker fees.

MBA agrees with these opinions and believes that broker fees must be separately itemized, and specifically labeled, so that consumers and regulators are able to discern whether the compensation paid to a mortgage broker is in fact reasonably related to the goods, services and facilities provided. Any disclosure approach that combines broker and lender compensation would undermine HUD's own analysis of the legality of broker fees. By separately disclosing broker and lender compensation, MBA's proposed forms are consistent with HUD's longstanding legal interpretations on this matter.

Finally, MBA notes that HUD spends considerable time in the preamble to its proposal discussing the consumer testing of its forms in general and the broker disclosure in particular. The purpose of this testing though was to avoid borrowers incorrectly selecting lenders versus brokers loan offers. This approach, however, assumed there were no differences between brokers and lenders. Considering all the distinctions identified in MBAs paper in Appendix D, MBA believes that borrowers need to understand both the functions and fees of lenders and brokers respectively. The tests conducted by HUD are not relevant to the panoply of concerns surrounding this issue. Considering that MBA and others hold otherwise, and believe that borrowers need better understanding of the functions and fees of lenders and brokers respectively, these test are not relevant concerning this issue. MBA strongly supports testing of the forms it proposes which make the respective fees clear and reference the mortgage broker fee agreement. It would also assist in the development of informational materials to make the broker's functions clear as well.

6. While MBA appreciates HUD's efforts to facilitate shopping, this aspect of the rule should not be finalized because of the difficulties of coordinating the concept with other laws. An alternative approach should be adopted (as discussed in 7 below).

The New Definition Is Inadvisable

While MBA appreciates HUD's efforts to facilitate shopping, the use of a new GFE application to elicit a binding GFE raises significant regulatory concerns and statutory questions. It is unnecessary to stop "sticker shock" at the settlement table based on differences between the GFE and the HUD-1.

The matter of bait and switch in consumer shopping could be better resolved by empowering consumers with a new Shopping Tool developed by HUD and the Board, along the lines proposed at Appendix C, that would elicit offers from lenders and mortgage brokers. As discussed in greater detail in 6 below, the matter of stopping unwarranted payment shock from the time of application to the time of closing can be addressed without changing the definition of "application."

The New Definition Would Raise Significant Regulatory Concerns

[32] 64 Fed. Reg. 10080 (March 1, 1999); 66 Fed. Reg. 53,052 (October 18, 2001).

The proposed revisions to the definition of "mortgage application" create significant concerns for lenders. The proposal would replace the definition currently found in RESPA's implementing regulation with two new definitions that, in effect, would bifurcate the mortgage application process into two distinct phases: the "GFE application" phase and the "mortgage application" phase. The impact of this redefinition has repercussions that extend well beyond RESPA, and may significantly alter legal and regulatory responsibilities under other laws and/or engender great confusion.

The term "mortgage application" is extremely important to RESPA's and TILA's disclosure regimes because it defines the start of the time period during which all initial consumer disclosures must be delivered. It is also important under other consumer protection statutes that regulate mortgage lending and employ "mortgage application" as the triggering event for disclosure or other requirements.

Specifically, changes in the definition of "application" would impact TILA and "Regulation Z,"[33] the Equal Credit Opportunity Act (ECOA) and "Regulation B,"[34] Home Mortgage Disclosure Act (HMDA) and "Regulation C,"[35] Fair Credit Reporting Act (FCRA) rules, and Section 311 of the Fair and Accurate Credit Transactions Act of 2003 (FACTA)[36] concerning the risk-based pricing notice.

The following list serves as a summary of the legal requirements that employ "application" as the triggering term:

- **Truth-In-Lending Act and "Regulation Z"**: TILA does not specifically define the term "application." Instead, the TILA regulations specifically adopt RESPA's definitions, stating that "creditors may rely on RESPA and Regulation X (including any interpretations issued by HUD) in deciding whether a 'written application' has been received." *Federal Reserve Board Regulation Z Official Staff Interpretations,* 12 C.F.R. § 226.19, 12 C.F.R. part 226 (Supp. I). *See also* 12 C.F.R. § 226.19.

- **Equal Credit Opportunity Act and "Regulation B"**: Regulation B defines a "loan application" as "an oral or written request for an extension of credit that is made in accordance with the procedures established by a creditor for the type of credit requested."[37] The *commentaries* to the regulations clarify that the actual practices followed by a creditor for making credit decisions, as well as its stated application procedures, will determine whether an application was actually made.[38]

- **Home Mortgage Disclosure Act and "Regulation C"**: HMDA requires that creditors report to the Federal Government the date that an "application" is received. Under HMDA's regulations, the definition for "application" is an "oral or written request for a home-purchase or refinance loan, or a refinancing that is made in

[33] 12 C.F.R. § 226.
[34] *See Federal Reserve Board Regulation B Official Staff Interpretations,* 12 C.F.R. § 202.2(f), Supp. I, comment 2.
[35] 12 C.F.R. § 203.2(b).
[36] Pub. L. No. 108-159 (December 4, 2003).
[37] 12 C.F.R. § 202.5(f).
[38] *See Federal Reserve Board Regulation B Official Staff Interpretations,* 12 C.F.R. § 202.2(f), Supp. I, comment 2.

accordance with procedures used by a financial institution for the type of credit requested.[39] The Regulation C commentary at Comment 2(b)-1 says that the Board interpretations that appear in the official staff commentary to Regulation B (Equal Credit Opportunity, 12 C.F.R. part 202, Supplement 1) are generally applicable to the definition of an application under Regulation C. However, under Regulation C the definition of an application does not include prequalification requests.[40]

- **Fair Credit Reporting Act**: Section 311 of the Fair and Accurate Credit Transactions Act of 2003 ("FACTA") provides that the risk-based pricing notice may be provided at the "time of application," when credit is granted, or when the approval is communicated to the consumer. Final rulemaking is still pending on the definitions and requirements of this provision.

HUD's proposal raises regulatory questions under these provisions because of its establishment of two separate and distinct definitions for the term "application." There now is no definitive answer regarding which of the two proposed definitions – GFE application or mortgage application – is the officially recognized trigger for the various statutory requirements. Each federal statute serves a different purpose, and, without clarification, each interpretation of a statute may diverge on how the time line for "application" should apply.

The HUD proposal is not clear and consistent on how other statutes are to apply. On the one hand, the proposed rule's preamble makes the statement that whether a GFE application "under a particular set of facts triggers HMDA or ECOA requirements must be determined under Regulation B and Regulation C, as interpreted by the Federal Reserve Board."[41] It also states that there have been "consultations with representatives of the Federal Reserve," and there are indications that the Board would prefer that early TILA disclosures be given in connection with the GFE application.[42] On the other hand, the proposed rule's Regulatory Impact Analysis makes a statement that expresses a two-pronged triggering mechanism for other federal statutes: (1) the definition of "application" for GFE and early TILA disclosures would be triggered by the GFE application; and (2) the requirements under Regulations B (ECOA) and C (HMDA) will be met when borrowers complete the application process by selecting a loan originator with whom his application will go forward.[43]

MBA agrees with HUD that the Board has final jurisdiction over the definitions required under the statutes it administers. In order to save considerable costs, these ambiguities must be resolved before this aspect of the rule is finalized, and not afterward in time consuming and expensive litigation.

HUD Need Not Establish the New Definition to Facilitate Shopping

Variations in costs from the time a borrower shops until the time they actually apply with a particular lender or mortgage broker is a different matter from closing cost shock at the time of

[39] 12 C.F.R. § 203.2(b).
[40] See 12 C.F.R. § 203.2(b).
[41] 73 Fed. Reg. 14036.
[42] Ibid.
[43] *See* 73 Fed. Reg. 14103.

settlement, where actual closing costs significantly vary from costs estimated at the time of mortgage application. The former, in MBA's view, is less of a problem and does not warrant revising the definition of application considering the foregoing regulatory concerns.

Many consumers today effectively shop among mortgage lenders. In order to facilitate the shopping by others among lenders and brokers, MBA supports the establishment of a new Shopping Tool to be developed by HUD and the Board, along the lines proposed by some members of MBA, and attached as Appendix C to these comments. Such a tool would elicit offers from lenders and mortgage brokers in the form of a non-binding GFE at Appendix A. The market would respond, as it does today, with relatively firm offers and the borrower could use the tool to narrow its search.

There is also some concern that shopping through a series of applications would adversely affect borrower's credit ratings. This concern would be obviated by the use of a shopping tool and non-binding GFEs.

Finally, going forward, HUD and the Board should make clear in informational materials that prices alone need not be determinative of a consumer's choice of a lender or mortgage broker. Borrowers do and should consider the quality of services provided, including, but not limited to, the particular lender's capacity and competence to provide responsive and prompt service to facilitate a timely, efficient and high quality lending experience.

7. While MBA supports methods to stem increases in fees from lenders and mortgage brokers from the time of application until settlement, it has serious concerns about HUD's proposal to limit lenders to a "zero tolerance" and to make them responsible for the charges of third-party providers. It believes retention of the "good faith" standard is consistent with the statute and that a bright line Borrower Protection approach should be established to help protect borrowers from fee increases.

While MBA supports greater protection for consumers against significant unjustified cost increases from the GFE at time of loan application to closing, it does not believe that the establishment of a zero tolerance for lender or broker fees is justifiable under RESPA or that a 10 percent tolerance on certain third party charges required by the lender or broker, as detailed below, is the best approach.

Problems with Establishing Tolerances

The proposed rule would prohibit lenders and brokers from exceeding the amount listed as "our service charge" on the GFE (provided in response to a preliminary GFE application) absent unforeseeable circumstances at time of closing. Under HUD's proposed rule, the "charge or credit for the interest rate chosen," if the interest rate is locked, also cannot be exceeded absent unforeseeable circumstances.

The proposed rule would also prohibit the sum of all the other settlement services subject to a tolerance from increasing by more than 10 percent. Such services include originator-required services where the originator selects the third party provider, originator-required services where the borrower selects from a list of third party providers identified by the originator, and optional owner's title insurance.

While MBA opposes unjustified increases in settlement costs at closing, the establishment of tolerances, in general, and restriction to a zero tolerance, in particular, for lender fees are legally questionable under RESPA. Section 5 of RESPA requires a "good faith estimate of the amount or range of charges for specific settlement services the borrower is likely to incur in connection with the settlement as prescribed by the Secretary."[44] While HUD asserts that the basis for its ability to impose tolerances is grounded in its ability to define the term "good faith," MBA does not believe that – considering the structure or legislative history of the statute – there is clear basis for tolerances and particularly a "zero tolerance."[45]

MBA does not believe that, as a general matter, lenders can or should be held responsible for the costs of third parties when lenders have no ability to control their costs. As more fully discussed below, the current proposal for volume discounts will not facilitate pricing arrangements that will be beneficial to the consumer. Lenders will not enter into volume discount arrangements if doing so causes them to face additional liability. MBA also believes that the establishment of a 10 percent tolerance overall on third-party charges recommended by the lender will likely prove counterproductive as long as the lender is held liable for violations of the tolerances. Lenders will simply not have the incentive to make any recommendations to the consumer of beneficial services.

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[44] 12 U.S.C. § 2604(c).

[45] The proposed amendments to the GFE are inconsistent with RESPA insofar as those amendments would impose tolerances or other specific standards for the accuracy of the GFE disclosure. The RESPA statute requires the lender to provide "a good faith *estimate* of the amount or range of charges for specific settlement services the borrower is likely to incur in connection with the settlement as prescribed by the Secretary." 12 USC 2604(c) (emphasis added). This is a requirement for an estimate of the settlement charges, not a requirement that these charges be disclosed with exact accuracy. Congress separately provided in RESPA for a final settlement statement for the charges actually imposed. 12 USC 2603. This requirement for a final settlement statement differs markedly from the GFE requirement by not stating that the disclosures could be provided as estimates. Because Congress provided separately for a final statement of settlement charges (in Section 4 of both the original RESPA and the current RESPA), and a "good faith estimate" of the settlement charges to be provided at the beginning of the loan application process, it seems clear that Congress did not contemplate that the GFE would be absolutely accurate.

The amendments at the enactment of RESPA are also instructive. The original RESPA statute stated that is was "the duty of the lender," when making the advance disclosure of settlement charges, "to obtain or cause to be obtained from persons who provide or will provide services in connection with such settlement the amount of each charge they intend to make." 12 USC 2605 (1974 version). Congress deleted this duty in its amendment to RESPA in 1976 when Congress added the formal GFE requirement. The RESPA statute has not changed in that regard since 1976 and still does not impose an affirmative duty on the lender to enter into binding relationships with third parties regarding the amount of such third parties' fees. While a lender must make a good faith effort to obtain accurate information as to the amounts of third party charges, that is quite different from a requirement that the disclosure of those amounts be accurate within regulatorily-specified tolerances.

Comparing RESPA to TILA, Congress expressly included accuracy standards and tolerances into TILA. See, for example, 15 USC 1605(f) and 1649(a)(3) (each providing accuracy tolerances for finance charges), and 15 USC 1606(c) (providing tolerances for the disclosure of the annual percentage rate). In contrast, Congress did not, however, impose or imply accuracy standards for GFE's.

Therefore, we believe that HUD's attempt to impose strict accuracy standards for the GFE is inconsistent with RESPA itself. Any such action by HUD would be in excess of HUD's statutory jurisdiction and authority, and a reviewing court therefore should hold such action to be unlawful and set it aside under the APA. 5 USC 706(2).

Additionally, MBA believes the establishment of a tolerance for government recording and transfer charges is unwarranted and presents unnecessary risks to lenders and to mortgage brokers.

While MBA notes that HUD has provided relief from the tolerances for unforeseeable circumstances, including acts of God and exceptions for other circumstances, MBA believes that these exceptions are too narrow considering the applicable statutory requirements. Section 5(c) of RESPA requires lenders to provide "a good faith estimate of the amount or range of charges for specific settlement services the borrower is likely to incur in connection with the settlement as prescribed by the Secretary [of HUD]." The proposal indicates that the tolerances would exclude acts of God or disaster or other type of emergency that makes it impossible or impracticable for the originator to perform or circumstances that could not be reasonably foreseen at the time of GFE application that are particular to the transaction and that result in increased costs such as change in the property purchase price, boundary disputes, or environmental problems that were not described to the loan originator in the GFE application; the need for a second appraisal and flood insurance.

Under this approach, by way of example, if a GFE is provided that reflects government recording and transfer charges that are based on the governmental unit's current fees, and later the governmental unit increases its charges, such an increase might be regarded as "unforeseeable" because governmental units increase fees from time to time. However, such an estimate would have been made in "good faith." Similarly, while price increases may be foreseeable they are may be unknown at the time of an "estimate" in "good faith."

MBA believes that the current regulations are more consistent with the current statute in requiring that estimates must be made in "good faith" and bear a "reasonable relationship" to the charge a borrower is likely to pay at settlement.[46] The rules should not require a lender to show that all increases are unforeseeable. What should be required is that the lender makes estimates based on information known to him in "good faith" at the time the estimates are made.

Finally, MBA does not believe there is a legal basis for RESPA rules requiring that when a loan application is rejected, and the tolerances are inapplicable, the borrower must be notified within one day. A one-day requirement is also unreasonable considering other workload constraints and, in MBA's view, it will present a particular hardship to small mortgage lenders and brokers. Moreover, before the rule is finalized, it must be harmonized with other provisions of law governing notice of denial (e.g., ECOA).

MBA's Alternative Approach: Borrower Protection Approach

As indicated, MBA believes a better approach under the current statute would be to apply the current regulatory standard for good faith estimates at 24 C.F.R. § 3500.7 which provides:

> *Each such estimate must be made in good faith and bear a reasonable relationship to the charge a borrower is likely to be required to pay at settlement, and must be based upon experience in the locality of the mortgaged property. As to each charge with respect to which the lender requires a particular settlement service provider to be used,*

[46] 24 C.F.R. § 3500.7(c).

the lender shall make its estimate based upon the lender's knowledge of the amounts charged by such provider.

The rules would then establish that HUD and other federal and state regulators would scrutinize lenders' good faith estimates for compliance unless lenders and brokers good faith estimates were in conformity with the Borrower Protection approach described below.

Under this approach, lenders and brokers would be deemed to be in good faith for any mortgage where (1) their own fees were no more than five percent greater at closing than estimated on the GFE at time of application and (2) estimated third party charges of providers required and selected or recommended by the originator were no more than 10 percent greater overall than estimated on the GFE.

MBA believes that the establishment of the Borrower Protection plan is a better approach than tolerances. Lenders and brokers will manage their businesses within Borrower Protections to assure that their estimates comply. At the same time, an approach along these lines would be more consistent with the statute and assure flexibility in unusual circumstances not contemplated by the rule.

Operationally, a borrower would first shop for a mortgage as he or she does today. The borrower could request a GFE from a lender or broker at that time but the estimate would not be binding and the tolerances would not apply. (The GFE that would be provided would be the same as the GFE used throughout the process (see below.)) Tolerances are unnecessary at this point. The market today responds to requests for GFEs at a preliminary stage with good offers. The problem that requires consideration is protecting borrowers from unjustified variations in costs between application and settlement.

Nonetheless, MBA strongly urges that HUD and the Board do much more to facilitate borrower shopping. As indicated, in 6 above, MBA believes that HUD and the Board should develop a Shopping Tool along the lines of the document in Appendix C to empower the consumer to ask the right questions about credit costs and settlement costs.

When the borrower is ready to apply for a mortgage, he or she would do so. The lender or broker would then provide a GFE either by delivering the good faith estimate, or by placing it in the mail to the loan applicant, not later than three business days after the application is received or prepared.

The GFE would be provided at no cost, except possibly for the cost of the credit report. MBA is mindful that the Board has proposed to require the early TILA disclosure without any significant fees and it supports the provision of a combined RESPA-TILA disclosure. However, in instances where the borrower wishes expedited treatment, the borrower should be allowed to provide a fee if he or she chooses an appraisal or a rate lock to expedite closing or to lock-in a rate. The ability to lock-in benefits borrowers and should not be unwittingly prevented under any new rules.

The GFE must be provided in good faith and would be subject to enhanced regulatory review. The foregoing five percent leeway on lender fees (including discount points and any charge for when a rate is locked) and a 10 percent overall window of certain costs (including title,

appraisals, and required services the lender or broker selects or recommends such as pest inspections) on the GFE would apply to lenders and mortgage brokers to assure that they meet the good faith standard. Under this approach, fee increases that exceed these Borrower Protection standards could be scrutinized by HUD or another applicable state or federal regulator to determine whether they are in good faith or whether they were not. Considering that government recording and transfer charges may change arbitrarily, they are outside MBA's proposed enhanced regulatory review and Borrower Protection requirements.
In applying the good faith standard, final costs explicitly may exceed the Borrower Protection amounts if: (1) the borrower requests a change in the loan product or amount by a bright line amount, $10,000 is suggested; or (2) acts of God occur; (3) any issues materially affecting the value of the borrower's credit or collateral are discovered; or (4) other circumstances occur such as increases in charges or fees that the lender or broker was not aware of at the time of its estimate in good faith.

Lenders and brokers will reissue the combined RESPA-TILA form following final underwriting at the time a commitment letter is sent to the borrower to reflect the results of final underwriting, including any applicable changes. Lenders and brokers will also issue an updated GFE as they often do today when the borrower changes the loan product or loan amount. Again, the GFE along with the TILA form at the pre-application stage, the application stage and the commitment stage will be the same form. Based on MBA's redesign, the forms will be readily comparable at each stage of the process.

MBA will continue to work at assuring the HUD-1 is available to borrowers the day before closing. For comparison purposes, borrowers will be advised to compare the GFE provided at loan approval to the HUD-1 to assure that the standard of good faith is met and that HUD may scrutinize increases that exceed the Borrower Protection standards.

8. The proposed changes to the HUD-1 to refer to the new GFE fail to achieve the objective of making the GFE and HUD-1 harmonious and readily comparable.

While laudable,
MBA does not believe that the changes to the HUD-1, in the form of relatively minor revisions and references to the GFE, are sufficient to make the forms truly comparable for the consumer. In fact, MBA believes that the introduction of the new closing script, which is intended to describe the relationship of the costs and terms on the GFE to those on the HUD-1, is at least in part an admission that the forms are not easily comparable. Considering that HUD's cost estimates for implementation of the GFE and HUD-1 forms are based on the comparability of these forms, MBA is convinced that these cost estimates are far too low.[47]

9. HUD should not Implement a "closing script" to be read at closing and to be signed by the borrower.

MBA does not believe that implementation of the closing scripts proposed by HUD, as an addendum to the HUD-1 or HUD-1A, is advisable. MBA believes its implementation would raise legal concerns, be too costly, provide little benefit to the consumer at closing and raise significant operational concerns. Moreover, the script itself is concerned with both loan terms

[47] 73 Fed. Reg. 14115-14116.

and settlement costs and as such should await the involvement of the Board as part of comprehensive RESPA-TILA reform, if it is to be implemented at all.

Notwithstanding the characterization of the script as an addendum to the HUD-1or HUD-1A, the script is an additional form to be prepared by the settlement agent, read to the borrower and signed at settlement which compares the loan terms and settlement charges on the GFE to the HUD-1. RESPA requires the HUD Secretary to develop and prescribe "a standard form for the statement of settlement costs which shall be used... as the standard real estate settlement form in all transactions in the United States which involve federally related mortgage loans."[48] While RESPA explicitly authorizes several other disclosures, the authority for establishing a closing script, which is in effect an additional disclosure, is not evident.

Just as important, MBA believes that the script will add unnecessary costs to the closing process. HUD itself estimates that the script will add 45 minutes of additional time per closing and estimates that cost at $54 (derived from a $150,000 salary.) HUD also says the costs in a normal year (based on 12.5 million originations) would be an estimated $676 million. It is not apparent, however, in reaching what MBA regards as an unusually low estimate, HUD fully considered all costs including the additional time for the lender, broker and others to assist in developing the script. There is also no apparent consideration of the considerable costs to borrowers considering the time the borrower must invest in this effort, e.g. lost wages.

For the consumer, closing is far too late to focus on a comparison of estimated and final loan terms and closing costs. It would be far better for the consumer to be provided a HUD-1, and a TILA disclosure prior to closing that was readily comparable to the GFE. Prior to closing, a consumer can question the lender or broker about charges and determine whether he or she will proceed with the loan.

Current RESPA regulations at 24 C.F.R. § 3500.10(a) permit the borrower to inspect the HUD-1 or HUD-1A settlement statement the business day immediately prior to settlement but the rules only require review of items that are known to the settlement agent at the time of inspection. Over the past few years, MBA, the American Land Title Association (ALTA) and the American Escrow Association (AEA) have been working together to develop uniform closing instructions. In their current form, these procedures, while not yet finalized, would, in part, enable borrowers to receive a complete HUD-1 a day before closing. MBA believes that, enhanced by a GFE that is truly comparable to the HUD-1, this effort holds far greater promise than the closing script to timely inform borrowers of closing costs and facilitate comparison with the GFE.

The script itself is focused as much on the rates and terms of the mortgage product chosen by the consumer as its settlement costs. For this reason alone, MBA would urge that if implementation is to be pursued further – and we do not believe it should be as proposed – it should be made part of a RESPA-TILA reform effort, coordinated with the Board.

Finally, use of such a script would present logistical problems in eMortgage transactions and in states where escrow closings are prevalent. The use of the script will either make these transactions unworkable and/or simply increase the paper required for borrower review. Also,

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[48] 12 U.S.C. § 2603(a).

considering that settlement agents must read the script and will be expected to answer questions, and will be expected to answer questions, the script's use may be impossible in states where there are statutes prohibiting the unauthorized practice of law.

10. MBA commends, with some modifications, HUD's proposal to clarify that lenders and brokers can use average cost pricing for settlement services within any class of transactions.

MBA commends HUD's proposal to exert its authority under Section 19 of RESPA to clarify that lenders and brokers can use average cost pricing for settlement services, with some clarifications and modifications. MBA has long sought explicit clarification of the legality of average cost pricing, not to increase industry profits but to facilitate pricing arrangements to reduce operational and compliance costs, and streamline operations all of which will result in lower costs to consumers. Average cost pricing methodologies permit tiered pricing arrangements where the average prices for third party services purchased in volume are lower than the prices for services purchased individually. These benefits are passed on to consumers in the market. Explicitly permitting these arrangements reduces legal risks resulting from requirements for precise price calculations.

MBA believes that with some modifications and clarifications, considering the benefits of average cost pricing, this proposal should be finalized even if the entire rule is not. In such event, MBA respectfully requests that HUD issue a policy statement or an interpretive rule for this purpose.

Specifically, the proposal would allow the average price for settlement services to be determined and disclosed based on either (1) the actual average price for the service on all loans closed by the "loan originator" on a national or more limited basis over the averaging period; or (2) the average price based on a tiered pricing contract for the service if the projected number of loans used in the calculation is equal to the actual number of loans actually closed during the averaging period.

The first circumstance identified above would require experience over a recent period of six consecutive months preceding the receipt of the GFE application as designated by the "loan originator." The second demands a tiered pricing contract during a retrospective averaging period. MBA believes that there should be additional flexibility to facilitate average cost pricing so that firms that do not fit into one of the two designated circumstances can still employ average cost pricing arrangements to benefit consumers.

MBA suggests that the rule include another approach or approaches that would be less restrictive and facilitate entry into average cost pricing for other firms to benefit consumers. MBA notes that several lenders who engage in average cost pricing are commenting on this rule. MBA urges HUD to look carefully at their comments on this subject (as well as other issues). Under one approach suggested, a firm would charge the average cost for a class of transactions over a prospective averaging period during which all transactions in the class would be charged a projected average price. As long as the total amounts charged on transactions in the class do not exceed the amount paid to the service providers for such transactions by more than a small amount (e.g., by more than 10 percent,) the average price would be permissible.

The proposal also provides that if a loan originator uses average cost pricing for "any class of transactions" in a particular period, the loan originator must use the same average cost price in every transaction within that class. The "loan originator" also must retain all documentation that the average cost pricing is "accurate" in a given time period under the pricing formula used for at least three years.

MBA believes that before this provision is finalized under a rule or an interpretative rule, the rule should be clarified to give maximum latitude to the lender to define a "class of transactions." Specifically, the lender should have latitude to broadly define a class based on type of service, type of property, loan type, and/or geographic region. The standard should be "a reasonably similar class of transactions" as defined by the lender. This approach would give the lender discretion to identify transactions such as valuations in a particular county or the subset of semi-detached homes in such county. Likewise, the lender should have latitude to define an "average period" and the "average price" as long as the approach is 'reasonable."

Finally, the documentation requirements should be revised to ensure that they are flexible and do not impede use of this provision by requiring unnecessarily burdensome documentation. The documentation should not be required to be retained to demonstrate "accuracy" but to support the lender's determinations.

11. While MBA commends HUD's proposal to clarify the legality of volume discounts, MBA believes the proposal is too restrictive.

MBA also commends HUD's proposal under Section 19 of RESPA to clarify that volume discounts are not prohibited, but does not believe it goes far enough. If it is modified, MBA believes that it also should be issued as an interpretative rule or clarification whether or not HUD goes forward with this rulemaking.

In its proposal, HUD redefined "thing of value," in connection with anti-kickback and referral fee provisions of Section 8, to exclude "discounts negotiated by settlement service providers based on negotiated pricing arrangements," provided that no more than the reduced price is charged the borrower and disclosed on the HUD-1 and HUD-1A.

Negotiated discount arrangements for services and materials result in lower costs to consumers and are therefore consistent with RESPA's purposes of lowering settlement costs. These arrangements achieve this objective in other industries, such as in the automobile industry where parts are ordered through volume arrangements. MBA does not believe RESPA was intended to or should impede similar discounting in the settlement services industry.

Nevertheless, by also including a requirement that no more than the reduced price can be charged to the borrower, MBA believes that there will be little incentive for lenders to enter into discount arrangements. Scrutiny to ensure that each and every dollar of discount is passed on to the consumer presents regulatory risks and will make the exception uninviting. Moreover, such a restriction is unnecessary. Market competition will result in the consumer receiving the benefit of discounts. If HUD is insistent about maintaining this provision, at the very least, HUD should make clear that "average cost pricing" can be employed in conjunction with volume

discounts. Under such an approach, it would be acceptable for the average price to be charged to the borrower, if permissible under the rules, rather than the fully discounted price.

MBA also questions the idea that discounts can only be negotiated by a settlement service provider, arguably excluding builders. MBA believes this approach could deprive consumers of negotiated discounts on house prices offered by lenders that have joint ventures and marketing agreements with builders.

While MBA recognizes that some small businesses do not support volume discounts, MBA is confident that small businesses will continue to thrive in the marketplace for settlement services as they do today and RESPA should not deprive consumers of the cost savings from volume discounts.

12. Concerning the proposed revisions to prohibitions against requiring the use of affiliates, MBA believes it would be sufficient for HUD to reaffirm that it may scrutinize discounts to ensure that they are *bona fide* rather than depriving borrowers of certain discounts altogether.

HUD proposes to change the definition of "required use" so an economic disincentive that a consumer can only avoid by purchasing a settlement service from an affiliated provider would be as problematic under RESPA as an incentive contingent on a consumer's choice of a particular provider. The proposed rule indicates that it is particularly directed to homebuilder affiliates but covers other affiliate situations.

MBA believes that the proposal in this area is too broad and may result in depriving borrowers of discounts that may indeed be *bona fide*. MBA believes it would be sufficient for HUD to indicate that under its current rules it may scrutinize discounts to assure they are *bona fide* rather than risking depriving borrowers of discounts altogether.

13. MBA generally supports HUD's efforts to update its RESPA regulations concerning mortgage servicing transfers and escrows and to explicitly recognize the applicability of ESIGN to RESPA.

MBA generally supports aspects of the proposed rule that would update the current RESPA regulations concerning the provision of the mortgage servicing disclosure statement within three days of a mortgage application and to remove outdated escrow provisions.

Specifically, these proposals would retain the initial mortgage servicing transfer notice but remove the requirement in the current rules that applicants for mortgage loans be provided a disclosure describing the lender's historical practice regarding the sale or transfer of servicing rights and sign the mortgage servicing transfer disclosure. The requirement for this aspect of the disclosure was removed by statute.[49] The proposal would also remove references to the phase-in period for the requirement of aggregate accounting for escrow accounts, which expired on October 12, 1997. Finally, the proposal also makes clear that that RESPA disclosures may be

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[49] Economic Growth and Regulatory Paperwork Reduction Act of 1996 (Title II of the Omnibus Consolidated Appropriations Act, 1997) (Pub. L. 104-208, §2103(a), 110 Stat. 3009).

provided in electronic form as long as the consumer consents to receive them in accordance with the provisions of the ESIGN Act.

MBA supports those clarifications that will conform the rules to current law and practice and thereby alleviate confusion in the real estate finance industry and among the consumers it serves, thereby reducing costs to companies large and small.

14. MBA will evaluate HUD's legislative proposals as they are developed in accordance with key principles to ensure transparency and facilitate the mortgage market.

In its proposal, HUD announced that it intends to seek legislative changes to: (1) authorize the Secretary to impose civil money penalties for violations of section 4 of RESPA (the Settlement Statement), section 5 (the GFE and Special Information Booklet), section 6 (servicing), section 8 (kickbacks, referral fees and unearned fees), section 9 (title insurance), and section 10 (escrows); (2) require delivery of the HUD-1 to the borrower three days prior to closing; and (3) expand and make uniform the statute of limitations applicable to governmental and private actions under RESPA.

There currently are some provisions under Sections 6, 8, 9 and 10 of RESPA to enforce those provisions but no appreciable enforcement authority exists under Sections 4 and 5. Nevertheless, state and federal regulators under a variety of laws do enforce these requirements. For this reason, as the proposals are developed, MBA will evaluate them carefully in the context of other authorities, including those under TILA, and the following principles:

- Disclosures should be streamlined and greatly simplified and uniform throughout the nation; terms that are not consumer friendly should be replaced with terms that are simple and understandable;
- Disclosures should be binding as early in the process as possible, considering that during the mortgage process information is developed and circumstances can change;
- The timing of disclosures should not result in undue delay for borrowers to receive needed credit;
- The process should facilitate competition to lower costs as well as the provision of high quality services;
- Borrowers and regulators should be appropriately empowered to prevent abuses;
- Lenders should have a reasonable opportunity to cure errors prior to litigation; and
- Remedies for errors should not result in unduly increased costs for all consumers.

Additionally, as indicated, MBA has been working to ensure that the HUD-1 is available one day prior to closing as part of its uniform closing instructions project. This effort can help ensure that borrowers all have an opportunity to view their HUD-1 the day before settlement. MBA is concerned, however, that requiring a disclosure three days prior to closing could unduly slow settlements and delay the provision of needed financing.

15. MBA supports an implementation schedule that would link implementation of this rule to the Board's forthcoming TILA reform rule.

Although, MBA strongly prefers combination of the TILA and RESPA efforts, as indicated, MBA believes the objective of minimizing costs can, to some extent, be achieved through an extended implementation period if HUD goes forward independently. In such event, MBA recommends that the implementation period for new forms and any aspect of the rule that requires retooling, systems changes or other significant costs should extend to 18 months after the rule's effective date or until the end of the implementation period for the Board's new rule, whichever is later.

III. RESPONSES TO SPECIFIC QUESTIONS

The proposal states that HUD welcomes comments on all aspects of the proposal. In addition, HUD specifically requests comment on the following issues:

1. and 2. Whether a 12-month implementation period for the GFE is appropriate. (Section IV.D.) The proposed GFE, as well as the proposed HUD–1/1A Settlement Statement Forms.

As stated, MBA favors an implementation period for any new forms beginning 18 months after the effective date of a final RESPA rule or 18 months after the implementation period for the Board's expected TILA rule, whichever is later. Requiring the industry to implement changes to RESPA disclosures and then to later implement changes to TILA disclosures would result in large and duplicative costs for systems changes, training and staffing that would be borne ultimately by consumers.[50] A *seriatim* approach to reform by HUD and then the Board would also result in considerable confusion and additional costs on the part of both consumers and the industry

3. Possible additional ways to increase consumer understanding of adjustable rate mortgages.

MBA appreciates HUD's interest in increasing consumer understanding of adjustable mortgages. MBA would point out, however, that the Board, other financial regulators, associations and individual companies have put considerable effort into this area and, for this reason, MBA believes that rather than "reinvent the wheel", this is an area where the various efforts should be built upon in close coordination with the Board, which has the primary responsibility in this area.

To the point, MBA believes that the TILA is the proper law to ensure that borrowers understand the nature of their credit terms and costs under their mortgage loans. MBA believes, for this reason, that RESPA reform pending Board involvement should be confined to closing costs. TILA and RESPA reform should converge so that borrowers have information on both credit and closing.

Notably, the Board has provided information on adjustable or variable rate mortgages under TILA. The Board has relatively recently updated its Consumer Handbook on Adjustable Rate-

[50] *See* page 3-15 of the Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis: Proposed Rule to Improve the Process of Obtaining Mortgages and Reduce Consumer Costs (March 14, 2008).

Mortgages (CHARM booklet) to reflect concerns about interest-only and payment option ARMs.[51] Pursuant to the Board's requirements, creditors are now required to provide information on the terms of adjustable loans.[52]

Additionally, the federal financial regulators have provided recent guidance on nontraditional mortgage products and subprime loans along with illustrations to help borrowers understand payment changes over the lives of loans so they can shop and compare mortgages.

MBA has also developed *The Simple Facts* and *the Simple Calculator,* which is available on its Home Loan Learning Center at www.homeloanlearningcenter.com. These tools explain and then demonstrate to borrowers how to predict present and future payments on adjustable rate mortgages. *The Simple Facts* and the interactive calculator have received enormous attention from those shopping for mortgages garnering approximately 1.5 million "hits" over the last year. MBA member companies also have invested considerable funds in the development of a wide range of educational materials and co-branded with MBA on these efforts.

Since disclosures regarding ARM loans raise different concerns from matters related to settlement costs under RESPA, it is an important that a consumer both understand the terms of credit as well as their settlement costs. However, for a range of reasons, including the Board's preeminence in this area, MBA strongly believes that HUD should follow the Board's lead in this area.

4. Whether the proposed requirements for completing and delivering the Addendum to the HUD–1/1A, including the mandatory reading of the Closing Script by the party conducting the closing to the borrower(s), are the best methods for assuring that borrower(s) understand their loan terms and the differences between the GFE and the HUD–1/1A.

As mentioned earlier in this comment letter, MBA does not believe that the closing script is well advised. Instead, MBA believes its implementation would raise legal concerns, be too costly, provide little benefit to the consumer at closing and raise significant operational concerns. Moreover, the script itself covers both loan terms and settlement costs and as such should await comprehensive RESPA-TILA reform, if it is to be implemented at all.

Once again, MBA believes it would beneficial to the consumer if the HUD-1 and GFE were truly comparable and if the complete HUD-1 were delivered to the consumer the day before closing so he or she may compare it to the GFE. It is, appropriately, the responsibility of the mortgage lender or mortgage broker to explain any cost differences between estimated and final costs. The closing agent should not be forced to step into the shoes of the lender and provide this costly and time consuming closing script.

As indicated, MBA is working with the American Land Title Association and the American Escrow Association to develop uniform closing instructions which in their present draft would assure a complete HUD-1 the day before closing.

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[51] The CHARM booklet was updated by the Board on December 26, 2006. The current booklet may be viewed at the following Web address: <http://www.federalreserve.gov/pubs/arms/arms_english.htm>.
[52] 73 Fed. Reg. 30997 (May 29, 2008).

5. Whether a provision should be added to the RESPA regulations allowing a loan originator, for a limited time after closing, to address the failure to comply with tolerances under the proposed GFE requirements, and if so, how should such a provision be structured? (Section IV.E. 10) Would such a provision be useful, and if so, what would be the appropriate time frame for finding and refunding excess charges? Could such a provision be abused, and therefore harmful to consumers? Would the ability of prosecutors to exercise enforcement discretion obviate the need for such a provision?

MBA strongly believes that a provision should be added to the regulations to allow lenders and mortgage brokers a limited time after closing to address the failure to comply with the tolerances as suggested above. Such procedures, in MBA's view, would be extremely useful and offer prompt relief to a borrower without costly litigation. If such a provision were included in the final rule, there should be sufficient time allotted to the lender or broker to review and correct the error. MBA would support a period of at least 90 days, after which enforcement or other action could be taken.

MBA does not believe such a provision would be abused. It would provide a short finite period during which the lender or mortgage broker has every incentive to correct any errors to eliminate the possibility of enforcement and/or legal action. The ability of prosecutors to exercise enforcement discretion would not obviate the need for this provision. Even in the best of circumstances, the attention of enforcement officials to particular matters will come too late to provide borrowers the prompt corrective action that rational cure provisions such as these could provide.

6. Proposed methods for calculating average cost prices and on any alternative methods that should be permitted (Section IV.H.), specifically, how to define "class of transactions." Comments are also invited on alternative average cost pricing methods and other pricing methods that benefit consumers and are based on factors that would lead to charges to the consumer and disclosure of such charges that are easily calculated, verified, and enforced, but difficult to manipulate in an abusive manner. Such factors could include: (a) Experience over a period of time that is longer or shorter than that currently provided in the proposed rule; (b) Prices for the service among the usual third party providers upon which the lender or other settlement service usually relies; (c) General industry practices; and (d) A reasonable projection of future costs.

As detailed above, MBA supports the proposal, with some clarifications and modifications, so lenders and brokers can use average cost pricing for settlement services to benefit consumers. MBA has long sought explicit clarification of the legality of average cost pricing, to facilitate pricing arrangements benefiting consumers, reduce operational and compliance costs, and to streamline operations. Average cost pricing methodologies permit tiered pricing arrangements where the average prices for third party services purchased in volume are lower than the prices for services purchased individually. Explicitly facilitating these arrangements reduces legal risks resulting from requirements for precise price calculations that serve to increase costs for consumers.

MBA requests that the final rule clarify that lenders may assign any "averaging" period as a "rolling," rather than a "static" period. Imposing a static six-month averaging period would, in effect, create "fee caps" that would severely hamper industry operations in times of inflation or excess demand. A "rolling" period, however, would allow lenders to more accurately reflect market prices in the provision of settlement services, because market shifts would be allowed to be incorporated slowly into current pricing models.

HUD should afford lenders maximum flexibility to define "class of transaction." We note that the market is dynamic and that any definition supplied by regulation will do nothing but calcify a classification that is likely to become obsolete in a short time. We also note that all public and private players involved in the administration and supply of mortgage capital – government, GSEs, investors, etc. – are currently restructuring operations and rethinking product categories in light of recent market events. Any definition that HUD adopts will become imprecise, even unusable, as market segments are redefined, new product categories introduced, and new regulations adopted.

For these reasons, the lender should have latitude to broadly define a class based on type of service, type of property, loan type, and geographic region. The standard should be "a reasonably similar class of transactions" as defined by the lender. This approach would give the lender discretion to identify transactions such as valuations in a particular county or the subset of semi-detached homes there.

This flexibility would adequately protect consumers. The rule would still provide guidance to assure that average cost pricing is reasonably based.

As mentioned before, MBA suggests that the rule include another approach or approaches that would be less restrictive and facilitate entry into average cost pricing for other firms to benefit consumers. Some MBA members commenting on this proposed rule will be offering alternatives. Under one approach suggested, a firm would charge the average cost for a class of transactions and a prospective averaging period during which all transactions in the class would be charged a projected average price. As long as the total amounts charged on transactions in the class do not exceed the amount paid to the service providers for such transactions by more than a small amount (e.g., by more than 10 percent, the average price would be permissible).

MBA requests further discussions on the documentation requirements that would be imposed on lenders under any final rule. The current proposal is scant on guidance that defines the precise documentation that HUD would require to demonstrate that the pricing is "accurate". MBA questions that standard. MBA respectfully requests that, if this aspect of this rule is finalized, HUD meet with the industry to craft a statement of policy that carefully sets forth documentation requirements in a way that ensures that lenders are not discouraged from using average cost pricing because of documentation requirements.

7. Whether the proposed change in the definition of "required use" will better serve the purposes of RESPA and whether further improvements could be made in the definition to accomplish the intent of both the affiliated business exemption in section 8 and the prohibition in section 9 on the required use of a title company. (Section IV.I.)

HUD proposes to change the definition of "required use" so an economic disincentive that a consumer can only avoid by purchasing a settlement service from an affiliated provider would be as problematic under RESPA as an incentive contingent on a consumer's choice of a particular provider. The proposed rule indicates that this provision is particularly directed to homebuilder affiliates but covers other affiliate situations.

MBA believes that this proposed amendment is a well-intentioned attempt to further the goals of RESPA. However, MBA believes that it would be sufficient for HUD to indicate that under its current rules HUD may scrutinize discounts and other special pricing or cost incentives to assure they are *bona fide*.

The reason for MBA's opposition to this aspect of the rule is that it has the real potential of precluding settlement service providers from offering *any* discounts, concessions, or benefits whatsoever. The amendments, as proposed, are too broad, and could be read to impose a penalty every time a provider offers a "special discount program" but withholds it from any consumer, even under fair and reasonable circumstances. In such an environment, a settlement service provider would not, for example, innovate to establish any conditions, stipulations, or restrictions around discount programs, because such conditions would run the risk of being interpreted as "disincentives" under the meaning of the proposed rule. "Conditions" for a benefit, and "disincentives," or "penalties" are fundamentally different concepts, but they would be indistinguishable in the RESPA context, as proposed. Rather than face these risks, providers would simply forego or eliminate these programs altogether, at great detriment to consumers, and contrary to the broad purpose of RESPA itself.

Again, MBA believes it would be sufficient for HUD to indicate that under its current rules, the Department may scrutinize discounts to assure they are *bona fide* and proper.

8. With respect to the revised definition of "Good Faith Estimate" set forth in the proposed rule language at 24 CFR 3500.2, is the standard set forth sufficient to ensure that good faith estimates will be filled out consistently by all loan originators in a particular community?

As indicated, while MBA does not concur in either the form of the GFE or the accompanying requirements proposed by HUD, the definition of "Good faith estimate or GFE" appears appropriate. The proposed rule provides that a GFE means "an estimate of settlement charges a borrower is likely to incur, as a dollar amount, and related loan information, based upon common practice and experience of the locality of the mortgaged property, provided on the form prescribed in Appendix C to this part that is prepared in accordance with the requirements at 3500.7 and the Instructions to Appendix A of this part." By incorporating the instructions – assuming they are clear as finalized – and requiring knowledge of practice and the experience of the locality, the definition should result in GFE forms being filled out consistently.

9. Should the Section 6 disclosure on transfer of servicing that is required under RESPA be included on the GFE?

No. In the interest of ensuring that the borrower is focused on what is most important on the GFE – the settlement costs – MBA strongly believes that the form should be directed to the best presentation of these costs and not cluttered with extrinsic information. While, the information

provided in the transfer of servicing disclosure may be relevant to some borrowers, it is not directly relevant to the borrower's costs and should be presented in a separate disclosure. As stated earlier, the new GFE already contains too much information that may confuse the borrower.

10. Should a loan originator be required to include a "no cost loan" on the trade-off chart on page 3 of the GFE as one of the alternative loans if it is not the loan for which the GFE is written?

No. MBA does not believe a comparison of "no cost loan" must be included in the GFE on page three. MBA believes information on alternative products could be included in additional pamphlets and/or on the shopping form prior to the application stage. It does not believe the trade-off chart should be included on the GFE.

IV. CONCLUSION

Again, MBA greatly appreciates the opportunity to provide comments to HUD on the subject rules. The Mortgage Bankers Association supports efforts to make the mortgage process simpler, clearer and more transparent for consumers. Doing so will empower consumers and help fight predatory lending. MBA does not believe the RESPA rule released by HUD is the right approach.

To ensure that we achieve a cohesive and improved disclosure methodology that is permanent, and protective of consumers, HUD and the Board must work together to reform their respective disclosures under RESPA and TILA in a comprehensive and complementary manner. Though inadvisable, if HUD goes forward independently, the rule should be pared down considerably and implemented on the same schedule as the Board's.

MBA looks forward to working with HUD and the Board to implement final regulations. For questions or further information, please do not hesitate to contact Ken Markison, Associate Vice President and Regulatory Counsel, at kmarkison@mortgagebankers.org or (202) 557-2930.

Sincerely,

Jonathan L. Kempner

Jonathan L. Kempner
President and Chief Executive Officer
Mortgage Bankers Association

Appendix A – Joint Combined RESPA-TILA Forms

Appendix B – MBA RESPA Forms

Appendix C – Consumer Shopping Tool

Appendix D – Mortgage Lenders and Mortgage Brokers

Appendix E – Summary of RESPA and the HUD Proposed Rule

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT [Optional language is in brackets] PAGE 1

Combined Good Faith Estimate of Settlement Costs and Truth in Lending Act Disclosure

Lender Name and Address	Mortgage Broker Name and Address	File Number
Buyer/Borrower Name and Address	Property Address	Date GFE Provided

Loan Description

Proposed Mortgage Loan Amount $________ ☐ Conventional ☐ FHA ☐ VA ☐ FSA/RHS

About this Combined Good Faith Estimate of Settlement Costs and Truth in Lending Act Disclosure

This disclosure contains a Good Faith Estimate of your settlement costs on page 1 and Truth in Lending disclosures of your loan's terms and costs on page 2 These are estimates based on information you provided. If your loan is approved, the estimated amounts may change based upon conditions discovered by the Lender in underwriting, or, if, among other things, you request a change in the loan amount, term, type of loan or lock your interest rate at a different time or on different terms.

Mortgage Loan Settlement Charges to Be Paid by You

The line numbers below correspond to the item numbers on the HUD-1 Settlement Statement you will receive at loan closing You should compare this Disclosure with the HUD-1 Statement you receive at closing to determine whether any changes have occurred and the reason for any changes Call your lender or mortgage broker with any questions.

Prepaid Finance Charges of $____ are included in the Settlement Charges shown below and are marked with an †. Your Prepaid Finance Charges together with interest and other lender-required loan related charges you will pay after closing (such as mortgage insurance premiums, if applicable) are shown on your Truth in Lending Disclosure as the Finance Charge.

800. Lender Origination Charges† (Line 801 plus 802 plus 803 less 804) $______

- **801 Lender Charges** for loan origination and other Lender services $____
- **802 Discount Points** paid to reduce your interest rate ____% $____
- **803 Rate Lock** paid to lock in your interest rate ____% $____
  (If you lock in your rate at a different time or on different terms, the lock fee may change See your Rate Lock Agreement for additional details.)
- **804 Lender Credit** for your choosing a higher interest rate ($____)

900. Mortgage Broker Origination Charges† (Line 901 less 902) $______

- **901 Total Broker Compensation** for Broker's services $____
- **902 Amounts Paid by Lender** to Broker on your behalf ($____)

Important Information When Using a Mortgage Broker. If you have agreed that the Lender may pay the Broker on your behalf part of the Total Broker Compensation (line 902), you will pay this amount through your loan's interest rate and monthly payment Your Mortgage Broker is required to enter into a Mortgage Broker Fee Agreement with you, which you should review

1000. Credit Report and Pre-Closing Appraisal and Inspection Charges $______
For credit reports, appraisals, property valuations, inspections, tax or flood determinations

1100. Title and Closing Charges (Sum of lines 1101–1105) $______

- **1101 Title Charges** $____
  (Lender's title insurance, survey, title examination, notary services, abstract or title search, documentation preparation)
- **1102 Owner's Title Insurance** with title coverage of $____ $____
- **1103 Closing Agent** to attend closing† $____
- **1104 Services Required** by closing agent but not by Lender $____
- **1105 Closing Agent Services** required by Lender† $____

1200. Government Recording & Transfer Charges $______

1300. Items Required by Lender to be Paid in Advance (Sum of lines 1301–1306) $______

- **1301 Daily Interest Charges†** from the day of your settlement until the first day of your normal payment cycle, estimated at $____ per day for 30 days $____
- **1302 Taxes** $____
- **1303 Hazard Insurance Premium** $____
- **1304 Flood Insurance Premium** $____
- **1305 Mortgage Insurance Premium†** $____
- **1306 Other (Specify)** ________ $____

1400. Initial Escrow Deposit† for escrow account to pay taxes, insurance, and other charges $______

☐ Mortgage insurance premium reserves of $____ are included in this amount

1500. Other Mortgage Loan Settlement Charges† such as life-of-loan flood and tax services, lender's attorney's fees, wire transfer and other miscellaneous services not covered above $______

1600. Total Estimated Mortgage Loan Settlement Charges $______

1700. Mortgage Loan Settlement Charges to be Paid by Borrower at Settlements $______
(Line 1600 less 1701 less 1702 less 1703)

- **1701 Amounts Paid by Borrower Before Closing** ($____)
- **1702 Amounts from Lender or Mortgage Broker** ($____)
- **1703 Settlement Charges Paid by Seller** ($____)

Note: In a purchase transaction the amount you will pay at settlement will be affected by whether the seller has agreed to pay any of the settlement charges, by the amount of your down payment, and by the amount you have already paid as a deposit Settlement charges paid by seller (line 1703) will appear on the HUD-1 Settlement Statement

You are entitled to shop for a limited number of settlement services. Check with your lender about the services you may shop for. These services and their charges are included in your Mortgage Loan Settlement Charges shown on line 1700 above; if you shop for these services, however, these amounts may change.

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT [Optional language is in brackets] PAGE 2

Combined Good Faith Estimate of Settlement Costs and Truth in Lending Act Disclosure

Lender Name and Address	Mortgage Broker Name and Address	File Number
Buyer/Borrower Name and Address	**Property Address**	**Date GFE Provided**

Loan Description

Proposed Mortgage Loan Amount $ ________ ☐ Conventional ☐ FHA ☐ VA ☐ FSA/RHS

About this Combined Good Faith Estimate of Settlement Costs and Truth in Lending Act Disclosure

This disclosure contains a Good Faith Estimate of your settlement costs on page 1 and Truth in Lending disclosures of your loan's terms and costs on page 2. These are estimates based on information you provided If your loan is approved, the estimated amounts may change based upon conditions discovered by the Lender in underwriting, or, if, among other things, you request a change in the loan amount, term, type of loan or lock your interest rate at a different time or on different terms

Annual Percentage Rate	Finance Charge	Amount Financed	Total of Payments
The cost of your loan as a yearly rate including interest as shown in the schedule below and other finance charges	The dollar amount the loan will cost you including Prepaid Finance Charges shown on page 1	Your Loan Amount less the Prepaid Finance Charges shown on page 1	The amount you will have paid after you have made all payments as scheduled
________ %	$ ________	$ ________	$ ________

Schedule of Interest Rates, Balances and Payments. Your loan has a term of ________ years, repayable as follows:

Interest Rate	Beginning Principal Balance	Number of Payments	Amount of Payment	Payments Due Monthly Beginning

Payment Increases. If checked below, your loan has features that may cause your payments to increase. Consider carefully whether you can afford to make the higher payments Do not assume that you will be able to refinance to lower your payments

☐ **Adjustable Rate:** Your loan contains an adjustable rate feature. See the Truth in Lending Act disclosures provided to you earlier about your adjustable rate feature. If the index used to adjust your interest rate increases, your actual interest rates and payments may be higher than shown above, but your interest rate will not increase above ________ % and your payments will not increase above $ ________

☐ **Interest Only:** The initial monthly payments cover only the interest on your loan amount. If you pay only interest due, after a certain period of time, your monthly payment will increase because you must pay back principal and interest

☐ **Negative Amortization:** You may be allowed to make payments on your loan that do not cover all of the interest owed. Unpaid interest owed will be added to your principal balance, increasing the amount that you must repay, but your principal balance will not increase above $ ________

☐ **Balloon Payment:** Your loan must be paid off in one large final payoff payment of up to $ ________ after ________ years

☐ **Demand Feature:** *The entire amount owed on this loan is payable on demand This means that the lender may require you to pay off your loan in full at any time* All disclosures are based on an assumed maturity of one year

Mortgage Insurance.

☐ **You will be required** to pay the cost of mortgage insurance for your loan. Any amounts you paid at or before closing are disclosed on page 1 and any costs you will pay after closing are included in the payments shown above

☐ **You will not be required** to pay mortgage insurance for your loan.

Payments for Taxes and Insurance. The payments shown above do not include amounts you will pay for real estate taxes and hazard insurance, estimated to be an additional $ ________ per month This amount is subject to change throughout the term of the loan.

☐ **Your loan provides** for an escrow account from which the lender will pay your taxes and insurance. Page 1 shows your initial escrow deposit. Monthly escrow payments will be required You will receive an escrow account statement no later than 45 days after settlement.

☐ **Your loan does not provide** for an escrow account You are responsible for paying taxes and insurance when due.

Prepayment.

☐ **Your loan has a prepayment charge.** If you pay off during the first [time period], you may have to pay a charge of up to $ ________.

☐ **Your loan has no prepayment charge.** If you pay off early, you will not have to pay a prepayment charge.

Hazard and Flood Insurance. You may obtain the required insurance from anyone you want that is acceptable to the lender.

Late Charge. If a payment is late, you will be charged $ ________.

Security. If you obtain this loan, the lender will have a mortgage on your home You could lose your home, and any money you have put into it, if you do not meet your obligations under the mortgage You are not required to obtain this loan merely because you have received these disclosures or have signed a loan application.

Assumption. Someone buying your house.

☐ **may, subject to conditions, be allowed** to assume the remainder of your mortgage on the original terms

☐ **will not be allowed** to assume the remainder of your mortgage on the original terms.

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT [Optional language is in brackets] PAGE 1

Combined HUD-1 Statement of Settlement Costs and Final Truth in Lending Act Disclosure

Lender Name and Address		**Mortgage Broker Name and Address**	
Buyer/Borrower Name and Address		**Seller Name and Address**	
Settlement Agent		**Property Address**	
Settlement Date	**Loan Number**	**File Number**	**MI Number**

Loan Description

Proposed Mortgage Loan Amount $ ________ ☐ Conventional ☐ FHA ☐ VA ☐ FSA/RHS

About this Combined HUD-1 Statement of Settlement Costs and Truth in Lending Act Disclosure

This disclosure contains a summary of the borrower's and seller's transaction on page 1, your settlement costs on page 2 and the final Truth in Lending Act disclosures of your loan's terms and costs on page 3 You can compare the estimated settlement costs on your Combined Good Faith Estimate of Settlement Costs and Truth in Lending Act Disclosure provided to you earlier to the final settlement costs on page 2.

A. Summary of Borrower's Transaction	**B. Summary of Seller's Transaction**
100 **Gross Amount Due from Borrower**	400 **Gross Amount Due to Seller**
101. Contract Sales Price	401. Contract sales price
102 Personal Property	402 Personal property
103 Net Settlement Charges to be Paid by Borrower (line 1700)	403
104	404
105	405
Adjustments for items paid by seller in advance	**Adjustments for items paid by seller in advance**
106. City/town Taxes to	406. City/town taxes to
107. County Taxes to	407. County Taxes to
108. Assessments to	408 Assessments to
109.	409
110.	410.
111.	411
112	412
120. **Gross Amount Due from Borrower**	420. **Gross Amount Due to Seller**
200 **Amounts Paid by or on behalf of Borrower**	500. **Reduction in Amount Due to Seller**
201 Deposit or earnest money	501. Excess deposit (see instructions)
202 Principal amount of new loan(s)	502 Net Settlement Charges to be Paid by Seller (line 1700)
203 Existing loan(s) taken subject to	503. Existing loan(s) taken subject to
204	504 Payoff of first mortgage loan
205.	505 Payoff of second mortgage loan
206	506
207.	507.
208.	508.
209	509.
Adjustments for items unpaid by seller	**Adjustments for items unpaid by seller**
210 City/town taxes to	510 City/town taxes to
211. County taxes to	511. County taxes to
212 Assessments to	512 Assessments to
213	513.
214.	514
215.	515
216.	516
217	517.
218	518.
219.	519.
220 **Total Paid By/For Borrower**	520 **Total Reduction Amount Due Seller**
300. **Cash at Settlement From/To Borrower**	600 **Cash at Settlement To/From Seller**
301 **Gross Amount Due from Borrower (line 120)**	601 **Gross Amount Due to Seller (line 420)**
302 Less Amounts paid By/For Borrower (line 220)	602. Less Reductions in Amount Due Seller (line 520)
303 Cash ☐ **From** ☐ **To** Borrower	603 Cash ☐ **To** ☐ **From** Seller

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT [Optional language is in brackets] PAGE 2

Combined HUD-1 Statement of Settlement Costs and Final Truth in Lending Act Disclosure

Lender Name and Address	**Mortgage Broker Name and Address**
Buyer/Borrower Name and Address	**Property Address**

C. Settlement Charges

Note: Prepaid Finance Charges of $_____ are included in the Settlement Charges shown below and are marked with an †. Your Prepaid Finance Charges together with interest and other lender-required loan related charges you will pay after closing (such as mortgage insurance premiums, if applicable) are shown on your Truth in Lending Disclosure as the Finance Charge

C-1. Real Estate Sale Settlement Charges	Column A Paid From Borrower's Funds at Settlement	Column B Paid From Seller's Funds at Settlement
700. Total Real Estate Commission — sales price $_____ at _____% A $_____ Division of Commission in 700 is as follows: 701. $_____ to _____ 702. $_____ to _____		
703. Real Estate Commission on line 700 paid at settlement	$_____	$_____
704. Other (specify) _____	$_____	$_____
C-2. Other Charges for Transactions Not Required by Broker or Lender		
750. Borrower's Attorney's Fee	$_____	$_____
751. Other (specify) _____	$_____	$_____
C-3. Mortgage Loan Settlement Charges to Be Paid by You		
800. Lender Origination Charges† (Line 801 plus 802 plus 803 less 804) 801. Lender Charges for loan origination and other Lender services $_____ 802. Discount Points paid to reduce your interest rate _____% / $_____ 803. Rate Lock paid to lock in your interest rate _____% / $_____ 804. Lender Credit for your choosing a higher interest rate ($_____)	$_____	$_____
900. Mortgage Broker Origination Charges† (Line 901 less 902) 901. Total Broker Compensation for Broker's services $_____ 902. Amounts paid by Lender to Broker on your behalf ($_____)	$_____	$_____
1000. Credit Report and Pre-Closing Appraisal and Inspection Charges (Appraisal, Credit Report, Tax or Flood Determination, Pre-closing Inspection, Pest Inspection)	$_____	$_____
1100. Title and Closing Charges (Sum of lines 1101–1104) 1101. Title Charges (Lender's Title insurance, Survey, Title examination, Notary services, Abstract or title search, Documentation preparation) $_____ 1102. Owner's Title Insurance (Coverage $_____) $_____ 1103. Closing agent to attend closing† $_____ 1104. Services required by the closing agent but not by the lender $_____ 1105. Closing agent services required by Lender† $_____	$_____	$_____
1200. Government Recording and Transfer Charges (Sum of lines 1201–1204) 1201. Recording fees Deed $_____ Mortgage. $_____ Releases. $_____ 1202. City/county tax stamps Deed. $_____ Mortgage $_____ 1203. State tax stamps Deed $_____ Mortgage $_____ 1204. Other government recording and transfer costs $_____	$_____	$_____
1300. Items Required by Lender to be Paid in Advance (Sum of lines 1301–1306) 1301. Daily Interest Charges from _____% to _____% at $_____ per day† $_____ 1302. Taxes $_____ 1303. Hazard insurance premium for _____ months at $_____ per month $_____ 1304. Flood insurance premium for _____ months at $_____ per month $_____ 1305. Mortgage insurance premiums for _____ months at $_____ per month† $_____ 1306. Other (specify) _____ $_____	$_____	$_____
1400. Initial Escrow Deposit for escrow account to pay taxes, insurance premiums and other charges (including mortgage insurance premiums† of $_____)	$_____	$_____
1500. Other Mortgage Loan Settlement Charges† required by lender (e.g., life-of loan flood service, wire transfers, lender's attorney's fee, life-of loan tax service, other miscellaneous services not shown above)	$_____	$_____
1600. Total Mortgage Loan Settlement Charges (Sum of amounts in Columns A and B)	$_____	$_____
1700. Net Settlement Charges to be Paid by Borrower at Closing (Line 1600 less 1701 less 1702 less 1703)(also entered on lines 103 and 502) 1701. Amounts Paid by Borrower before Closing $_____ (specify item numbers) _____ 1702. Amounts from Lender or Mortgage Broker $_____	$_____	$_____
1703. Settlement Charges Paid by Seller (specify item numbers)	$_____	

Borrower: compare the amounts for each category (including the amounts the seller has agreed to pay, if any) with the amounts for each category shown on your Good Faith Estimate of Settlement Costs.

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT [Optional language is in brackets] PAGE 3

Combined HUD-1 Statement of Settlement Costs and Final Truth in Lending Act Disclosure

Lender Name and Address	Mortgage Broker Name and Address
Buyer/Borrower Name and Address	**Property Address**

Annual Percentage Rate	Finance Charge	Amount Financed	Total of Payments
The cost of your loan as a yearly rate including interest as shown in the schedule below and other finance charges	The dollar amount the loan will cost you including Prepaid Finance Charges shown on page 2	Your Loan Amount less the Prepaid Finance Charges shown on page 2	The amount you will have paid after you have made all payments as scheduled
______ %	$ ______	$ ______	$ ______

Schedule of Interest Rates, Balances and Payments. Your loan has a term of ______ years, repayable as follows:

Interest Rate	Beginning Principal Balance	Number of Payments	Amount of Payment	Payments Due Monthly Beginning

Payment Increases. If checked below, your loan has features that may cause your payments to increase Consider carefully whether you can afford to make the higher payments Do not assume that you will be able to refinance to lower your payments

☐ **Adjustable Rate:** Your loan contains an adjustable rate feature See the Truth in Lending Act disclosures provided to you earlier about your adjustable rate feature If the index used to adjust your interest rate increases, your actual interest rates and payments may be higher than shown above, but your interest rate will not increase above ______ % and your payments will not increase above $ ______

☐ **Interest Only:** The initial monthly payments cover only the interest on your loan amount. If you pay only interest due, after a certain period of time, your monthly payment will increase because you must pay back principal and interest

☐ **Negative Amortization:** You may be allowed to make payments on your loan that do not cover all of the interest owed. Unpaid interest owed will be added to your principal balance, increasing the amount that you must repay, but your principal balance will not increase above $ ______

☐ **Balloon Payment:** Your loan must be paid off in one large final payoff payment of up to $ ______ after ______ years.

☐ **Demand Feature:** The entire amount owed on this loan is payable on demand This means that the lender may require you to pay off your loan in full at any time. All disclosures are based on an assumed maturity of one year.

Mortgage Insurance.

☐ **You will be required** to pay the cost of mortgage insurance for your loan Any amounts you paid at or before closing are disclosed on page 2 and any costs you will pay after closing are included in the payments shown above

☐ **You will not be required** to pay mortgage insurance for your loan.

Payments for Taxes and Insurance. The payments shown above do not include amounts you will pay for real estate taxes and hazard insurance, estimated to be an additional $ ______ per month This amount is subject to change throughout the term of the loan

☐ **Your loan provides** for an escrow account from which the lender will pay your taxes and insurance. Page 2 shows your initial escrow deposit Monthly escrow payments will be required. You will receive an escrow account statement no later than 45 days after settlement.

☐ **Your loan does not provide** for an escrow account You are responsible for paying taxes and insurance when due.

Prepayment.

☐ **Your loan has a prepayment charge.** If you pay off during the first [time period], you may have to pay a charge of up to $ ______.

☐ **Your loan has no prepayment charge.** If you pay off early, you will not have to pay a prepayment charge

Hazard and Flood Insurance. You may obtain the required insurance from anyone you want that is acceptable to the lender

Late Charge. If a payment is late, you will be charged $ ______

Security. If you obtain this loan, the lender will have a mortgage on your home You could lose your home, and any money you have put into it, if you do not meet your obligations under the mortgage You are not required to obtain this loan merely because you have received these disclosures or have signed a loan application

Assumption. Someone buying your house:

☐ ***may, subject to conditions, be allowed*** *to assume the remainder of your mortgage on the original terms*

☐ **will not be allowed** to assume the remainder of your mortgage on the original terms.

Borrower Signature	Date	Borrower Signature	Date

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT [Optional language is in brackets] PAGE 1

Good Faith Estimate of Settlement Costs

Lender Name and Address	Mortgage Broker Name and Address	File Number
Buyer/Borrower Name and Address	**Property Address**	**Date GFE Provided**

Loan Description

Proposed Mortgage Loan Amount $________ ☐ Conventional ☐ FHA ☐ VA ☐ FSA/RHS

About this Good Faith Estimate of Settlement Costs

This disclosure contains a Good Faith Estimate of your settlement costs on page 1 These are estimates based on information you provided If your loan is approved, the estimated amounts may change based upon conditions discovered by the Lender in underwriting, or, if, among other things, you request a change in the loan amount, term, type of loan or lock your interest rate at a different time or on different terms.

Mortgage Loan Settlement Charges to Be Paid by You

The line numbers below correspond to the item numbers on the HUD-1 Settlement Statement you will receive at loan closing. You should compare this Disclosure with the HUD-1 Statement you receive at closing to determine whether any changes have occurred and the reason for any changes Call your lender or mortgage broker with any questions

Prepaid Finance Charges of $_____ are included in the Settlement Charges shown below and are marked with an † Your Prepaid Finance Charges together with interest and other lender-required loan related charges you will pay after closing (such as mortgage insurance premiums, if applicable) are shown on your Truth in Lending Disclosure as the Finance Charge.

800. Lender Origination Charges† (Line 801 plus 802 plus 803 less 804) $________

- **801 Lender Charges** for loan origination and other Lender services $_____
- **802 Discount Points** paid to reduce your interest rate _____% $_____
- **803 Rate Lock** paid to lock in your interest rate _____% $_____
  (If you lock in your rate at a different time or on different terms, the lock fee may change See your Rate Lock Agreement for additional details)
- **804 Lender Credit** for your choosing a higher interest rate ($_____)

900. Mortgage Broker Origination Charges† (Line 901 less 902) $________

- **901 Total Broker Compensation** for Broker's services $_____
- **902 Amounts Paid by Lender** to Broker on your behalf ($_____)

Important Information When Using a Mortgage Broker. If you have agreed that the Lender may pay the Broker on your behalf part of the Total Broker Compensation (line 902), you will pay this amount through your loan's interest rate and monthly payment Your Mortgage Broker is required to enter into a Mortgage Broker Fee Agreement with you, which you should review

1000. Credit Report and Pre-Closing Appraisal and Inspection Charges $________
For credit reports, appraisals, property valuations, inspections, tax or flood determinations.

1100. Title and Closing Charges (Sum of lines 1101–1105) $________

- **1101 Title Charges** $_____
  (Lender's title insurance, survey, title examination, notary services, abstract or title search, documentation preparation)
- **1102 Owner's Title Insurance** with title coverage of $_____ $_____
- **1103 Closing Agent** to attend closing† $_____
- **1104 Services Required** by closing agent but not by Lender $_____
- **1105 Closing Agent Services** required by Lender† $_____

1200. Government Recording & Transfer Charges $________

1300. Items Required by Lender to be Paid in Advance (Sum of lines 1301–1306) $________

- **1301 Daily Interest Charges**† from the day of your settlement until the first day of your normal payment cycle, estimated at $_____ per day for 30 days $_____
- **1302 Taxes** $_____
- **1303 Hazard Insurance Premium** $_____
- **1304 Flood Insurance Premium** $_____
- **1305 Mortgage Insurance Premium**† $_____
- **1306 Other (Specify)** ____________ $_____

1400. Initial Escrow Deposit† for escrow account to pay taxes, insurance, and other charges $________

☐ Mortgage insurance premium reserves of $_____ are included in this amount

1500. Other Mortgage Loan Settlement Charges† such as life-of-loan flood and tax services, lender's attorney's fees, wire transfer and other miscellaneous services not covered above $________

1600. Total Estimated Mortgage Loan Settlement Charges $________

1700. Mortgage Loan Settlement Charges to be Paid by Borrower at Settlements $________
(Line 1600 less 1701 less 1702 less 1703)

- **1701 Amounts Paid by Borrower Before Closing** ($_____)
- **1702 Amounts from Lender or Mortgage Broker** ($_____)
- **1703 Settlement Charges Paid by Seller** ($_____)

Note: In a purchase transaction the amount you will pay at settlement will be affected by whether the seller has agreed to pay any of the settlement charges, by the amount of your down payment, and by the amount you have already paid as a deposit Settlement charges paid by seller (line 1703) will appear on the HUD-1 Settlement Statement.

You are entitled to shop for a limited number of settlement services. Check with your lender about the services you may shop for. These services and their charges are included in your Mortgage Loan Settlement Charges shown on line 1700 above, if you shop for these services, however, these amounts may change.

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT [Optional language is in brackets] PAGE 1

HUD-1 Statement of Settlement Costs

Lender Name and Address		**Mortgage Broker Name and Address**	
Buyer/Borrower Name and Address		**Seller Name and Address**	
Settlement Agent		**Property Address**	
Settlement Date	**Loan Number**	**File Number**	**MI Number**

Loan Description

Proposed Mortgage Loan Amount $ ________ ☐ Conventional ☐ FHA ☐ VA ☐ FSA/RHS

About this HUD-1 Statement of Settlement Costs

This disclosure contains a summary of the borrower's and seller's transaction on page 1 and your settlement costs on page 2. You can compare the estimated settlement costs on your Combined Good Faith Estimate of Settlement Costs and Truth in Lending Act Disclosure provided to you earlier to the final settlement costs on page 2.

A. Summary of Borrower's Transaction	**B. Summary of Seller's Transaction**
100. Gross Amount Due from Borrower	**400. Gross Amount Due to Seller**
101 Contract Sales Price	401. Contract sales price
102 Personal Property	402. Personal property
103 Net Settlement Charges to be Paid by Borrower (line 1700)	403
104	404.
105	405
Adjustments for items paid by seller in advance	**Adjustments for items paid by seller in advance**
106 City/town Taxes to	406. City/town taxes to
107 County Taxes to	407 County Taxes to
108 Assessments to	408 Assessments to
109	409
110	410
111.	411
112	412
120. Gross Amount Due from Borrower	**420 Gross Amount Due to Seller**
200 Amounts Paid by or on behalf of Borrower	**500 Reduction in Amount Due to Seller**
201 Deposit or earnest money	501 Excess deposit (see instructions)
202. Principal amount of new loan(s)	502 Net Settlement Charges to be Paid by Seller (line 1700)
203 Existing loan(s) taken subject to	503. Existing loan(s) taken subject to
204.	504 Payoff of first mortgage loan
205	505 Payoff of second mortgage loan
206	506
207.	507
208.	508
209	509
Adjustments for items unpaid by seller	**Adjustments for items unpaid by seller**
210. City/town taxes to	510 City/town taxes to
211 County taxes to	511 County taxes to
212 Assessments to	512 Assessments to
213	513
214	514.
215	515.
216	516
217	517.
218	518
219	519
220. Total Paid By/For Borrower	**520 Total Reduction Amount Due Seller**
300 Cash at Settlement From/To Borrower	**600 Cash at Settlement To/From Seller**
301. Gross Amount Due from Borrower (line 120)	**601. Gross Amount Due to Seller (line 420)**
302. Less Amounts paid By/For Borrower (line 220)	602 Less Reductions in Amount Due Seller (line 520)
303 Cash ☐ **From** ☐ **To** Borrower	603 Cash ☐ **To** ☐ **From** Seller

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT [Optional language is in brackets] PAGE 2

HUD-1 Statement of Settlement Costs

Lender Name and Address	**Mortgage Broker Name and Address**
Buyer/Borrower Name and Address	**Property Address**

C. Settlement Charges
Note: Prepaid Finance Charges of $_______ are included in the Settlement Charges shown below and are marked with an † Your Prepaid Finance Charges together with interest and other lender-required loan related charges you will pay after closing (such as mortgage insurance premiums, if applicable) are shown on your Truth in Lending Disclosure as the Finance Charge

C-1. Real Estate Sale Settlement Charges	**Column A** Paid From Borrower's Funds at Settlement	**Column B** Paid From Seller's Funds at Settlement
700. Total Real Estate Commission — sales price $________ at ______% A $________		
Division of Commission in 700 is as follows:		
701. $ ________ to ________		
702. $ ________ to ________		
703. Real Estate Commission on line 700 paid at settlement	$ ________	$ ________
704. Other (specify) ________	$ ________	$ ________
C-2. Other Charges for Transactions Not Required by Broker or Lender		
750. Borrower's Attorney's Fee	$ ________	$ ________
751. Other (specify) ________	$ ________	$ ________
C-3. Mortgage Loan Settlement Charges to Be Paid by You		
800. Lender Origination Charges† (Line 801 plus 802 plus 803 less 804)	$ ________	$ ________
801. Lender Charges for loan origination and other Lender services $ ______		
802. Discount Points paid to reduce your interest rate ______% / $ ______		
803. Rate Lock paid to lock in your interest rate ______% / $ ______		
804. Lender Credit for your choosing a higher interest rate ($ ______)		
900. Mortgage Broker Origination Charges† (Line 901 less 902)	$ ________	$ ________
901. Total Broker Compensation for Broker's services $ ______		
902. Amounts paid by Lender to Broker on your behalf ($ ______)		
1000. Credit Report and Pre-Closing Appraisal and Inspection Charges (Appraisal, Credit Report, Tax or Flood Determination, Pre-closing Inspection, Pest Inspection)	$ ________	$ ________
1100. Title and Closing Charges (Sum of lines 1101–1104)	$ ________	$ ________
1101. Title Charges (Lender's Title insurance, Survey, Title examination, Notary services, Abstract or title search, Documentation preparation) $ ______		
1102. Owner's Title Insurance (Coverage $ ______) $ ______		
1103. Closing agent to attend closing† $ ______		
1104. Services required by the closing agent but not by the lender $ ______		
1105. Closing agent services required by Lender† $ ______		
1200. Government Recording and Transfer Charges (Sum of lines 1201–1204)	$ ________	$ ________
1201. Recording fees Deed. $ ______ Mortgage. $ ______ Releases. $ ______		
1202. City/county tax stamps Deed. $ ______ Mortgage. $ ______		
1203. State tax stamps Deed: $ ______ Mortgage $ ______		
1204. Other government recording and transfer costs $ ______		
1300. Items Required by Lender to be Paid in Advance (Sum of lines 1301–1306)	$ ________	$ ________
1301. Daily Interest Charges from ______% to ______% at $ ______ per day† $ ______		
1302. Taxes $ ______		
1303. Hazard insurance premium for ______ months at $ ______ per month $ ______		
1304. Flood insurance premium for ______ months at $ ______ per month $ ______		
1305. Mortgage insurance premiums for ______ months at $ ______ per month† $ ______		
1306. Other (specify) ________ $ ______		
1400. Initial Escrow Deposit for escrow account to pay taxes, insurance premiums and other charges (including mortgage insurance premiums† of $ ______)	$ ________	$ ________
1500. Other Mortgage Loan Settlement Charges† required by lender (e g , life-of loan flood service, wire transfers, lender's attorney's fee, life-of loan tax service, other miscellaneous services not shown above)	$ ________	$ ________
1600. Total Mortgage Loan Settlement Charges (Sum of amounts in Columns A and B)	$ ________	$ ________
1700. Net Settlement Charges to be Paid by Borrower at Closing (Line 1600 less 1701 less 1702 less 1703)(also entered on lines 103 and 502)	$ ________	$ ________
1701. Amounts Paid by Borrower before Closing $ ______ (specify item numbers) ________		
1702. Amounts from Lender or Mortgage Broker $ ______		
1703. Settlement Charges Paid by Seller (specify item numbers)	$ ______	

Borrower: compare the amounts for each category (including the amounts the seller has agreed to pay, if any) with the amounts for each category shown on your Good Faith Estimate of Settlement Costs.

Note: 1 page front/back – To be provided in English and a few other languages.

IMPORTANT INFORMATION REGARDING MORTGAGE PRODUCTS

This document explains some basic terms of loan products available, and provides a tool for you to use to shop and compare products. Be sure to understand your loan terms, including any fees/charges that apply. Seek any professional help you need to understand your loan terms, such as a lawyer, accountant, or translator. If you have any questions, contact your loan officer or mortgage broker. Before you choose your loan, be sure that you know the answers to the following questions about your loan. You can use the attached chart to compare loan products

- **Can my monthly principal & interest payment go up over time? By how much and how often?**

Payment Increases can occur for many reasons, many of which are more fully described below. If you can't make the payments when due, you could lose your property Even if you are eligible to refinance your loan at that time, you will have to pay refinance expenses, your payments and interest rate may increase, and the number of payments remaining may increase. If your property has gone down in value or if you don't have enough equity in your property, you may find it more difficult or more expensive to refinance or to obtain cash back at the sale of your property.

- **Can my interest rate go up over time? By how much and how often?**

Adjustable Rate Mortgages (ARMs) have rates that change over time. The rate is made up of two numbers: an "index" and a "margin". The index is usually found in newspapers or on the Internet, and it changes over time. The margin is an additional amount that usually doesn't change. The lender calculates your rate by adding the index and margin together. ARMs may start with rates that are lower than fixed rate loans, but over time, the rate and payment can go higher.

- **Can my loan balance go up, even if I make all payments in full and on time?**

Negative Amortization Mortgages permit the loan balance to increase, even if you make the minimum payments. Negative amortization prevents you from building equity, and can even leave you owing more than the property is worth Eventually, the reduced payment ends, and your payment will increase

- **Will any scheduled payment exceed the normal monthly payment?**

Balloon Payments are payments that exceed the normal monthly payment, sometimes significantly.

- **Will my normal payment cover only interest at any point during the loan term?**

Interest Only Payments cover only the interest accrued on the loan balance during the month, and do not reduce the outstanding loan balance. As a result, they are lower than payments that include principal. Interest only payments last only for a certain period of time, after which, your monthly payment will increase.

- **Will my normal payment include taxes, assessments and insurance (referred to as "escrow payments")? If not, will I pay a fee for not including escrow payments in my monthly payment?**

Escrow Accounts are special cash reserves that you pay to your lender, which the lender uses to pay taxes, insurance, or other charges related to the property. The lender will add the additional "escrow amount" to your regular loan payment, and annually, will adjust the amount upward or downward to reflect increases or decreases in these costs. In some situations, the lender may waive this escrow account requirement. If the lender waives the requirement, your monthly payment will be reduced, but the lender may charge an additional cost for agreeing to do so, and you will still have to pay the taxes, insurance and other charges yourself.

- **If I choose to provide the lender with less than complete documentation of my income or assets, will I pay additional costs?**

Reduced Documentation Loans limit the information you must give the lender in order to be approved (such as pay-stubs or tax returns). The lender instead relies on your statements about income or assets. While this feature may be convenient, the lender may charge a higher rate and/or extra fees for offering it.

- **Will I have to pay a fee if I pay off the loan in full ahead of schedule? Will I have to pay a fee if I pay more than the required monthly payment? (See information on prepayments below.)**

Prepayment Fees are fees for paying ahead of schedule. Some apply only if you pay off the full balance. Others apply anytime you make a payment that exceeds your scheduled payment. A prepayment fee will make it more expensive for you to sell or refinance the property

- **Will I pay an additional fee if my payments are late? How much?**

Late Fees apply when you do not make a payment on time. Your lender may, or may not, give you a "grace period", during which you can pay late without incurring a late fee.

- **What is my initial interest rate and what are my settlement charges?**

Lower interest rates may have higher settlement charges, and higher interest rates may have lower settlement charges. Be sure to understand both the rate and the settlement charges, and choose the best package for you.

- **What Are Discount Points? Should I Buy Discount Points? How Many?**

Discount Points are fees paid to the lender at closing in order to lower your mortgage interest rate and monthly mortgage payment. The cost of each point is equal to 1% of the loan amount As a rule of thumb, the mortgage's interest rate is reduced by ¼ percentage point for every discount point you pay. The actual amount, however, varies by lender. Whether or not paying points makes sense depends in part on how long you plan to keep the loan.

Note: 1 page front/back – To be provided in English and a few other languages.

LOAN COMPARISON CHART – Only you can decide upon the best loan for you. As you shop for the loan that best fits your needs, use this chart to compare loan products, fees and terms. Use additional pages to compare more products.

Borrower Name: **Property Address:**	**Loan 1**	**Loan 2**	**Loan 3**	**Loan 4**
Product Type (ARM, Fixed, Interest Only, etc.)				
Loan Amount				
Loan Term				
Once I lock in an interest rate, how quickly must I close the loan to take advantage of the locked rate?				
What are my total estimated settlement charges?				
What amount of my total estimated settlement charges is made up of points?				
How will my interest rate be affected by discount points?				
What is the initial interest rate?				
Can the interest rate rise? Be sure to understand by how much and how often the interest rate can rise.				
What is the maximum interest rate?				
What is the initial monthly payment (including principal, accrued interest, but excluding taxes, assessments and any property or mortgage insurance)?				
Can the monthly payment go up over time? Be sure to understand by how much and how often the monthly payment can rise.				
Will any scheduled payment exceed the normal monthly payment?				
Will my normal payment cover only interest at any point during the loan term?				
Will my normal payment include taxes, assessments and property insurance? Be sure to understand if any additional costs will be incurred for not including escrow payments.				
Will my loan require mortgage insurance? Be sure to understand how much and how the premium will be paid.				
Can my loan balance go up, even if I make all payments in full and on time?				
Will I have to pay a fee if I pay off the loan in full ahead of schedule or if I pay more than the required monthly payment? Be sure to understand the amount of any prepayment fee and how it is calculated.				
Will I pay an additional fee if my payments are late? Be sure to understand the amount of any late fee and when the fee is due.				
If I choose to provide the lender with less than complete documentation of my income or assets, will I pay additional costs?				

This is not a commitment to make a loan to you or to offer the terms or costs that may be filled in by you or any one else in the chart above. In order to obtain any specific loan, you must first submit a loan application, pay any required application fees, as well as, lock your rate and terms, and pay any required lock fees.

MORTGAGE BANKERS ASSOCIATION

MORTGAGE BANKERS AND MORTGAGE BROKERS:

DISTINCT BUSINESSES WARRANTING DISTINCT REGULATION

MORTGAGE BANKERS ASSOCIATION®
Investing in communities

Executive Summary

For many consumers, buying a house is the biggest financial investment they will make. The mortgage process, however, can be both complex and confusing, with a broad menu of loan offerings and a puzzling multitude of actors. Among those actors are mortgage bankers and mortgage brokers. While there is some superficial similarity in how they interact with consumers, mortgage bankers and mortgage brokers conduct very different businesses. These differences, however, are not well understood, creating confusion that can lead to inappropriate regulatory approaches.

To support policymakers working to improve the mortgage market, the Mortgage Bankers Association (MBA) has prepared this Issue Paper explaining the functional, financial, and regulatory differences between mortgage bankers and mortgage brokers. MBA believes that these differences warrant distinct regulatory approaches. Accordingly, policymakers and regulators must understand and properly consider these differences as they explore measures to increase transparency in the mortgage process, protect consumers from steering and abuse, and ensure that consumers are the beneficiaries of the lower homeownership costs that a free and fair market can produce.

Based on the distinctions set out below, this paper also proposes legal and regulatory changes that would provide borrowers with clearer information about mortgage brokers' responsibilities and compensation, improve brokers' financial accountability and strength, and ensure that loan originators are appropriately licensed and meet rigorous standards of professionalism.

Mortgage bankers and mortgage brokers perform different functions

- **Brokers are intermediaries between borrowers and mortgage bankers.**

Mortgage brokers typically have access to the loan offerings of numerous mortgage bankers. They inform borrowers of loan choices, receive loan applications, and perform certain services, such as collecting documentation, and initiating credit and other reviews.

Mortgage brokers turn loans over to mortgage bankers for underwriting and funding.

- **Mortgage bankers provide funds for mortgages.**

Mortgage bankers purchase and fund loans arranged by mortgage brokers and by other mortgage bankers. To do so, mortgage bankers use their own funds, funds they borrow, or funds they receive from secondary market investors. As part of the funding process, mortgage bankers are responsible for loan underwriting and, correspondingly, have a significant financial stake in a loan's performance.

Additionally, mortgage bankers often originate loans through their own retail sales force, informing borrowers about available loan products and working with borrowers through the lending process.

Mortgage bankers may also service loans, collecting and processing monthly payments and handling other ongoing customer service needs. Servicers, along with other mortgage bankers that sell loans into the secondary market, have ongoing responsibilities to investors.

Consumers have different expectations of mortgage bankers and mortgage brokers

- **Consumers perceive brokers as "trusted advisors."**

Consumers working with mortgage brokers generally rely on the broker, as an intermediary with access to multiple mortgage bankers' products, to identify the best loan product(s) for them. Consumers expect that mortgage brokers are comparison shopping on their behalf.

Mortgage brokers frequently perpetuate this expectation by promoting themselves as "trusted advisors," even though brokers in most cases have no legal obligation to act in borrowers' best interests.

- **Consumers look to mortgage bankers for information about their product offerings and the application process.**

When consumers work directly with mortgage bankers in obtaining a loan, they view the mortgage banker as a knowledgeable source of information about their own loan products and the mortgage

process. Consumers generally will compare mortgage bankers' loan offerings with those of other mortgage bankers and/or mortgage brokers.

Mortgage banker and mortgage broker compensation differs

■ **Brokers are paid to arrange loans and they receive compensation at the time the loan is made.**

A mortgage broker is compensated at the time a loan is closed through fees directly charged to the borrower (direct fees) and payments from mortgage bankers (indirect fees), which vary based on a loan's interest rate and/or other loan pricing terms. Indirect fees, known as yield spread premiums (YSPs), generally are greater when the loan's interest rate is greater.

YSPs, when used properly, can help borrowers pay their up-front closing costs, including broker fees, by building them into the interest rate. When a consumer does not understand the YSP, which is often the case, the risk is greater that the YSP will simply augment the broker's direct fees and saddle the borrower with a higher rate and monthly payment.

■ **Mortgage bankers receive revenue in several ways throughout the life cycle of a loan.**

Mortgage banker compensation can come throughout the life of a loan from:

- Origination fees;
- Interest payments;
- Servicing fees;
- Proceeds from the sale of servicing rights; and/or
- Proceeds from the sale of a loan.

Differences between mortgage banker and mortgage broker compensation mean different financial incentives

■ **Brokers' compensation has the potential to incentivize brokers to put borrowers into more expensive and/or inappropriate loans.**

Because broker compensation is directly tied to a loan's interest rate and brokers lack an ongoing financial stake in loan performance, brokers have a high incentive to get loans closed, maximize fees for origination, and move on to their next transaction. Furthermore, the current lack of understanding about YSPs makes it easier for some brokers to direct consumers toward loans with higher interest

rates and other terms, such as prepayment penalties, that increase the loans' value to a mortgage banker or investor.

- **Mortgage bankers' financial successes are linked to loan performance, giving mortgage bankers a stake in borrowers' ongoing ability to repay their loans.**

Mortgage bankers also are financially motivated to make loans. Origination fees, however, are but one of several sources of mortgage banker revenue. Mortgage banker revenue can come from multiple revenue streams associated with managing various risks throughout the life of a loan, including the risk that the borrower defaults.

Whether they hold loans or sell them to investors, mortgage bankers generally lose money when loans default. As a result, mortgage bankers have a greater interest in ensuring that borrowers choose products that will give them long-term financial success.

Mortgage bankers and mortgage brokers are subject to different disclosure requirements, with broker fee disclosures inadequate for effective consumer shopping

- **Current disclosures do not adequately inform borrowers of the connection between a broker's compensation and a loan's interest rate or the terms of the mortgage selected.**

While Real Estate Settlement Procedures Act (RESPA) rules require mortgage brokers to disclose the amount of their direct fees received from the borrower and the amount of any YSP received from the mortgage banker, current YSP disclosures do not explain adequately the connection between the YSP and a loan's interest rate.

As a result, consumers lack sufficient information to effectively shop among brokers and mortgage bankers and their various loan offerings. Both the U.S. Department of Housing and Urban Development (HUD) and the Federal Reserve are concerned about this problem and are trying to address it through proposed regulations to clarify YSP disclosures and enhance consumer understanding of the connection between YSPs and interest rates.

- **Mortgage bankers' costs and fees related to origination — such as processing and underwriting fees, as well as discount points and origination fees — are disclosed as settlement costs.**

RESPA regulations do not require mortgage bankers to disclose loan officer compensation and payments the mortgage banker might receive, such as gains (or losses) on secondary market sales of loans. This difference is appropriate because consumers do not rely on mortgage bankers and their loan officer employees as "trusted advisors" in the same manner as they do with mortgage

brokers. Additionally, payments related to a secondary market transaction are not always known with certainty at the time of settlement.

Barriers to market entry differ and are greater for mortgage bankers

- **Becoming a mortgage banker requires a significantly larger commitment of financial and other resources than becoming a mortgage broker.**

A mortgage banker must have capital to fund loans, or access to credit, such as through a warehouse line of credit. Moreover, to maintain and renew its license or charter, a mortgage banker must have a specified level of net worth and/or regulatory capital.

Mortgage brokers generally are not required to have funding sources or net worth except in nominal amounts.

Mortgage bankers and mortgage brokers are subject to different types and levels of regulatory oversight

- **Mortgage bankers are subject to greater supervision and regulation than brokers, and broker regulation is uneven across the nation.**

Mortgage bankers are subject to many complex state and federal laws that impose substantial penalties for noncompliance. Whether they are depository or non-depository institutions, mortgage bankers are routinely examined and audited by both federal and state regulators.

Mortgage bankers who sell loans to investors are subject to investor-required oversight. This oversight can include periodic reviews covering financial and business operations, origination practices, and financial safety and soundness. Similarly, mortgage bankers making loans insured by the Federal Housing Administration (FHA) are subject to oversight by HUD.

Mortgage broker licensing laws are uneven,[1] with brokers overall subject to less comprehensive and less demanding legal and regulatory oversight.[2]

Recommendations

The fundamental differences in consumer expectations, market incentives, and regulatory oversight call for distinct approaches to improving mortgage broker and mortgage banker regulation. Because improving consumer protection and enhancing market functions and transparency can be best

1 See *State by State Tally of Mortgage Broker Rules*, www.bankrate.com, http://www.bankrate.com/brm/news/mtg/20010104b.asp

2 See Lloyd T. Wilson, Jr., *A Taxonomic Analysis Of Mortgage Broker Licensing Statutes: Developing a Programmatic Response to Predatory Lending*, 36 N.M.L. REV. 297 (Spring 2006).

achieved through proposals that recognize these differences and address areas of weak or ineffective regulation, MBA supports measures requiring that:

- Borrowers receive clear disclosures of brokers' responsibilities and compensation;
- Mortgage brokers who claim to be or act as borrower agents be treated legally as agents;
- Mortgage brokers have sufficient financial resources — through a national minimum net worth requirement — to provide protection to borrowers and mortgage bankers where necessary;
- Mortgage brokers be appropriately bonded to give consumers greater protection; and
- All loan originators, including mortgage brokers and mortgage bankers, be appropriately licensed and registered in accordance with rigorous standards.

The current turmoil in the mortgage market and the credit markets has spurred efforts by regulators and policymakers to examine the causes and identify the right approaches to protect consumers and improve market functions and transparency. MBA supports these efforts. Policymakers, however, should avoid broad brush efforts that do not consider the complexity of the marketplace and the differing roles and responsibilities of mortgage brokers and mortgage bankers. MBA believes that measures which improve the regulation of mortgage brokers and other loan originators by addressing specific regulatory and oversight weaknesses are likely to improve the market for consumers, mortgage bankers, mortgage brokers, and other mortgage professionals and not produce barriers to efficient market operations.

MBA looks forward to working with Congress, regulators, and its industry partners to improve the marketplace and to improve the housing industry's ability to serve America's homebuyers.

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Introduction

The past two decades have been unprecedented for the U.S. housing market. Homeownership has reached historically high rates, borrowers have had access to a greater variety of loan products and features than ever before, and the breadth and complexity of the mortgage markets have increased exponentially.

At the same time, the mortgage brokerage industry has emerged and grown tremendously. According to the National Association of Mortgage Brokers (NAMB), there are over 25,000 mortgage brokerages in the United States.[3] Close to 50 percent of residential mortgage loans in the U.S. market are originated by independent mortgage brokers.[4] At the height of the recent boom of the subprime mortgage market, 70 to 80 percent of nonprime loans are estimated to have been mortgage broker originations.[5]

Mortgage brokers have become key intermediaries in expanding access to mortgage credit, including for communities traditionally underserved by mainstream financial institutions. Through mortgage brokers, mortgage bankers have expanded product reach, and thus served larger numbers of consumers.

3 http://www.namb.org/namb/About_NAMB.asp?SnID=1841827686. See also *Mortgage Brokers Fall on Tough Times*, USA Today (August 30, 2007).

4 MBA Research Data Notes, *Residential Mortgage Origination Channels*, September 2006.

5 Ibid.

Although mortgage bankers' and mortgage brokers' roles may be complementary, mortgage bankers and brokers perform distinctly different functions. The differences between mortgage banking and mortgage brokerage, however, are not well understood, possibly because mortgage bankers and brokers interact extensively in the mortgage process.

Some representatives of the mortgage brokerage industry have added to the confusion by proposing identical standards for mortgage brokers and mortgage bankers because both are "loan originators." They assert that there should be a "level playing field" on which brokers and mortgage bankers should compete for consumer business. MBA shares the goal of ensuring robust competition in the mortgage market place. However, a "one size fits all" approach to regulation is not the same as achieving a level playing field and ignores the fact that there are profound differences between the two industries warranting distinctive regulation.

This paper reviews the distinctions between mortgage bankers and mortgage brokers. The most critical distinctions are that mortgage brokers and mortgage bankers:

- Perform different functions and provide different services;
- Create vastly different expectations in borrowers;
- Are compensated differently;
- Have very different financial incentives;
- Face much different barriers to marketplace entry, with brokers facing very low barriers to entry; and
- Are subject to different regulatory requirements with bankers generally subject to more stringent regulation and oversight.

Considering the profound differences between mortgage bankers and mortgage brokers, this paper concludes with recommendations for regulatory improvements to enhance consumer understanding and information in the loan origination process, and to promote greater mortgage broker accountability.

Differences Between Mortgage Bankers and Mortgage Brokers

Mortgage Bankers and Mortgage Brokers Perform Different Functions in the Mortgage Process

■ Brokers Act as Intermediaries between Consumers and Mortgage Bankers

Mortgage brokers are independent intermediaries who bring together prospective borrowers and mortgage bankers. According to NAMB, a mortgage broker has "a working relationship with numerous banks and other mortgage bankers and provides the consumer with access to hundreds of options when it comes to financing a home."[6] Mortgage brokers tend to be small businesses and frequently have little capital.

Mortgage brokers help arrange loans, performing application-related services, such as requesting verification of the borrower's employment, requesting credit and other information, and compiling borrower documentation.[7] Brokers typically do not provide loan funds.[8]

Brokers can — and do — provide substantial benefits to borrowers and mortgage bankers and contribute to the efficiency of the mortgage industry. Brokers are an important distribution channel for

6 http://www.namb.org/namb/Mission.asp?SnID=1411867994

7 Until recently, brokers often arranged for property appraisals. Freddie Mac and Fannie Mae recently announced several changes in their appraisal requirements, including a new policy that prohibits brokers from selecting or compensating appraisers. See http://www.fanniemae.com/media/pdf/030308_agreement.pdf

8 In most instances, the mortgage broker assigns the mortgage to the mortgage banker at settlement and the mortgage broker is paid for his or her origination services. This process is known as "table funding."

mortgage bankers' loan products and, in particular, can enhance mortgage bankers' ability to serve traditionally underserved borrowers and communities.

■ Mortgage Bankers Provide Mortgage Funds

Mortgage bankers lend money through various channels: directly to consumers through their own retail sales forces, by funding loans arranged by brokers or other mortgage bankers, and by purchasing loans originated by other mortgage bankers. In most cases, mortgage bankers offer their own products.[9] Regardless of the lending channel, mortgage bankers are responsible for underwriting the loan, which involves evaluating the borrower's credit worthiness and the value of the home.

Once a loan is funded, mortgage bankers — depending on their business models — pursue various paths. Some mortgage bankers hold the loans in their own portfolios; others sell the loan to a secondary market investor. Separately, a mortgage banker may service the loan or sell the servicing rights.

Mortgage banking is highly competitive — mortgage bankers compete with each other and at times, with mortgage brokers, for customers. Nearly 8,900 mortgage lenders reported under HMDA in 2006.[10] Mortgage bankers compete for consumers through price, products, and services. Mortgage bankers seek to offer attractive interest rates and loan terms and to develop innovative loan products and services to meet a variety of consumer mortgage needs. Additionally, if a mortgage banker services loans, they provide continuous customer service and support to borrowers during the life of the loan.

Mortgage bankers are organized in many forms, such as federal- and state-chartered banks, thrifts, credit unions, and other depository institutions, as well as non-depository mortgage companies. Mortgage bankers come in many different sizes, from small businesses to large multinational corporations.

Differing Functions of Mortgage Bankers and Brokers Lead to Vastly Different Consumer Expectations

The different functions and services of mortgage bankers and mortgage brokers lead consumers to have vastly differing expectations of each. Consumer expectations of mortgage brokers often do not match brokers' actions and responsibilities, which effectively limits the consumer's ability to protect his or her own interests.

9 Mortgage bankers sometimes function as mortgage brokers, offering the loan products of other, larger mortgage bankers. Where a mortgage banker performs the function of a mortgage broker, MBA believes that the banker should be subject to the same disclosure requirements as a broker.

10 Robert B. Avery, Kenneth P. Brevoort, and Glenn B. Canner, "The HMDA Data," *Federal Reserve Bulletin*, December 2007. http://www.federalreserve.gov/pubs/bulletin/2007/pdf/hmda06final.pdf

■ Consumers Perceive Brokers as Acting in the Consumer's Best Interest

Consumers expect mortgage brokers to act as independent advisors and work with various mortgage bankers to identify and evaluate various financing options and ultimately to arrange their loans. In their marketing, brokers often position themselves as "trusted advisors" who will shop among mortgage bankers and arrange for the best loan. A 2003 AARP survey of older borrowers who had obtained refinancings found that 70 percent of respondents with broker-originated refinance loans (compared with 52 percent of respondents with lender-originated loans) reported that they had relied "a lot" on their brokers to find the best mortgage for them.[11]

Brokers' legal obligations, however, do not match up with consumer perceptions. While a consumer expects a broker to act in the consumer's interests, unless state law[12] or written agreement exists to the contrary, brokers are not legally considered their customers' agents. Comments in the Federal Reserve Board's recent Truth in Lending Act (TILA) regulatory proposal,[13] which requires compensation agreements between brokers and consumers, address this point and the concerns it raises:

> "Several commenters in connection with the Board's 2006 hearings suggested that mortgage broker marketing cultivates an image of the broker as a 'trusted advisor' to the consumer. Consumers who have this perception may rely heavily on a broker's advice, and there is some evidence that such reliance is common...
>
> If consumers believe that brokers protect consumers' interests by shopping for the lowest rates available, then consumers will be less likely to take steps to protect their own interests when dealing with a broker. For example, they may be less likely to shop rates across retail and wholesale channels simultaneously to assure themselves the broker is providing a competitive rate. They may also be less likely to shop and negotiate brokers' services, obligations, or compensation up-front, or at all. For example, they may be less likely to seek out brokers who will promise in writing to obtain the lowest rate available."[14]

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11 Kellie K. Kim-Sung & Sharon Hermanson, *Experiences of Older Refinance Mortgage Loan Borrowers: Broker- and Lender-Originated Loans,* Data Digest #83 (AARP Public Policy Inst., Washington, D.C.), Jan. 2003, at 3, available at http://www.aarp.org/research/credit-debt/

12 A handful of state mortgage broker licensing laws — including Vermont, Kentucky, Minnesota, Maine, and North Carolina — create some level of agency-principal relationship between mortgage brokers and their customers. See Lloyd T. Wilson, *A Taxonomic Analysis of Mortgage Broker Licensing Statutes: Developing a Programmatic Response to Predatory Lending,* 36 N.M.L. REV. 297, 325-339 (Spring, 2006).

13 Truth in Lending; Proposed Rule, 73 FED. REG. 1672, 1699 (request for comment January 9, 2008).

14 Ibid.

■ **Consumers View Mortgage Bankers as Offering a Set of Products**

When a consumer deals with a mortgage banker, he or she looks to the mortgage banker as a knowledgeable source of information about its' own products. Consumers expect a mortgage banker (through its employee loan officers) to explain the features of its loan product offerings and to provide assistance through the application and closing process. However, a borrower seeking to obtain a mortgage directly from a mortgage banker likely will research and compare different mortgage bankers' prices and products. As noted above, a borrower using a broker generally delegates the research and comparison of loan products to the broker.[15]

The Federal Reserve's recent TILA proposal reaches the same conclusion about consumer expectations and behavior:

> "The [Federal Reserve] Board is not aware of significant evidence that consumers perceive mortgage bankers' employees the way they often perceive independent brokers — as trusted advisors who shop for the best loan for a consumer among a wide variety of sources. Accordingly, it is not clear that a key premise of the proposal to restrict creditor payments to brokers — that consumers expect a broker has a legal or professional obligation to give disinterested advice and find the consumer the best loan available — holds true for creditor payments to their own employees."[16]

Compensation to Mortgage Bankers and Mortgage Brokers Differs, with Broker Compensation Presenting Greater Risks of Steering

Mortgage banker and broker compensation are based on the rate and terms of loans. However, mortgage banker and mortgage broker revenue and profit drivers are very different, reflecting the different services performed and financial risks borne by each:

- Mortgage brokers are paid solely for sourcing and facilitating loans, and they bear little — if any — ongoing financial risk.
- Mortgage bankers receive a variety of payments at the time of origination and after for performing a variety of services and managing a complex set of risks.

When coupled with ineffective consumer information about broker compensation, the "upfront" nature of broker compensation and its link to the borrower's interest rate pose greater risks of steering

15 The tendency to rely (to the consumer's financial detriment) on a mortgage broker can be especially strong for borrowers either from traditionally underserved market segments or with blemished credit. See Kenneth R Harney, *Study of Loan Fees Shows All Borrowers Not Equal*, The Washington Post, July 19, 2003, at F01.

16 73 FED. REG. at 1699.

than the mortgage banking business's more varied and complicated revenue streams. Those banker revenue streams, as discussed below, are closely linked to loan performance.

■ Brokers Are Paid for Sourcing and Originating Loans and Bear Virtually No Financial Responsibility for Loan Performance

The most common compensation model for mortgage brokers is a combination of fees paid or financed by the prospective borrower at loan closing (direct fees) and fees paid to the broker by the mortgage banker (indirect fees). Direct fees are typically loan origination or similar charges paid by borrowers at settlement. Once the loan is funded, brokers bear little — if any — ongoing risk. Brokers bear some risk if there is fraud in the loan documents and for very early loan payoffs (typically, within the first 90 to 180 days),[17] but the extent of that liability generally is only as large as the brokers' fees.[18]

Indirect fees are payments from the mortgage banker to the broker for origination services and are based on the rate of the loan and/or other loan pricing features. These payments are commonly called "YSPs" or "yield spread premiums." The YSP is the present value of the difference between the interest rate that the broker obtained for the loan and the lowest rate the mortgage banker would have accepted for the specific transaction (the "par rate"). The greater the spread between the rate on the specific loan and the par rate, the greater the YSP. Loan pricing features that increase the value of a mortgage loan, such as prepayment fees, may also increase YSPs.

The mortgage broker receives the YSP from the mortgage banker. However, consumers pay for the YSP through higher interest rates and higher monthly payments. Where YSPs are understood, they can provide a useful option for consumers to pay the broker's direct fees and other closing costs as part of the mortgage by essentially building them into the loan rate and payments.

■ Many Mortgage Bankers Receive Compensation throughout the Life of a Loan and Are Financially Accountable for Loan Performance

Mortgage bankers earn revenue in several ways, including through fees for services related to loan origination and underwriting. Borrowers pay these fees at closing or may choose to finance some or all of these fees. The borrower may also pay the mortgage banker "points" to reduce further the interest rate on the mortgage loan.

17 The duration of a broker's liability for early payoffs depends on the specific terms of a broker's contract with a lender.

18 In the case of early payoffs, most wholesaler agreements require the broker to forfeit some or all of his fees. Wholesaler agreements normally provide that the broker is liable for repurchase in the case of fraud. However, repurchases rarely occur due to brokers' limited capital. As a fallback, wholesalers will seek an indemnification from the broker that he/she will reimburse for any losses incurred on the loan; this usually ends up taking the form of some or all of the brokers' fees.

A mortgage banker who holds the loan in its portfolio receives interest payments from the monthly payments over the life of the loan. A mortgage banker holding a loan in portfolio must manage and hedge against both the interest rate and credit risk associated with the loan; correspondingly, the mortgage banker's financial gain or loss is linked to the success of that risk management.

Mortgage bankers also realize gains (or losses) on the sale of mortgages when loans are pooled and sold to investors in the secondary mortgage market. A secondary market sale and the corresponding financial outcome, however, are not always a certainty at the time a loan is closed. Constant fluctuations in the market, shifting interest rates and unpredictable investor appetites for mortgages mean that there is no assurance that mortgage bankers can sell loans to investors at a profit.

Additionally, selling a loan to a secondary market investor does not fully eliminate the financial risks to the mortgage banker. When selling a loan to a secondary market investor, the mortgage banker ordinarily guarantees to the investor that the loan and borrower credit characteristics are as stated to the investor and that the loan complies with relevant legal and regulatory requirements, including applicable anti-fraud and anti-predatory lending laws and guidelines. Typically, mortgage bankers are bound contractually to buy back non-performing loans[19] found to be inconsistent with these representations and warranties. This is an on-going financial risk that the mortgage banker bears.

Mortgage bankers who service loans (known as "servicers") also earn servicing fees. However, a servicer only earns these fees as long as the borrower is making timely payments. A loan's servicing rights can be sold separately from the loan itself. A mortgage banker who sells a loan's servicing rights has ongoing financial exposure through representations and warrants made to the buyer of the servicing.

■ Profit Drivers for Brokers Increase the Likelihood of Steering

Studies indicate that the fees charged to borrowers for origination activities, such as application processing and underwriting rarely result in profits for mortgage bankers.[20] Instead, these fees offset the mortgage banker's costs of processing and underwriting a loan application. Other loan-related fees, such as fees for credit reports and appraisals, are required to cover only the actual out-of-pocket costs for items provided by third party vendors, such as credit reporting agencies and appraisal companies and the costs of reviewing them. They therefore do not provide profit for mortgage bankers. The vast majority of mortgage banking income comes from interest, loan servicing, and, where loans are profitably sold in the secondary market, asset sales.[21]

19 A "non-performing" loan is a loan that is delinquent or in default.

20 See Mortgage Bankers Association, *2007 MBA Cost Study*, at 10–12.

21 Ibid.

In contrast, origination and origination-related fees and YSPs are the main profit centers for mortgage brokers. Mortgage brokers do not generally have continuing business relationships with their borrower clients after loan closing (unless it is to refinance their loan or obtain another mortgage at a later date). Unlike brokers of other financial products, such as independent insurance agents, mortgage brokers do not receive additional compensation based on loan performance or have other meaningful incentives to assure such performance.

The importance of YSPs as a source of broker revenue, coupled with the fact that YSPs are not well understood, increases the risk that some mortgage brokers will steer borrowers to costlier mortgages because they provide the mortgage broker with more lucrative YSPs.

The difference in a mortgage banker's degree of control over a loan officer employee versus a mortgage broker also makes it easier for mortgage brokers to steer borrowers into unnecessarily costly loans. Mortgage bankers have a variety of means for monitoring their loan officer employees and disciplining loan officers engaged in inappropriate steering. While mortgage bankers can — and do — refuse to do business with mortgage brokers engaged in inappropriate steering and other unprofessional practices, mortgage brokers' independence and the fact that mortgage bankers are not present as mortgage brokers work with borrowers and shop loans makes monitoring difficult.

Mortgage Bankers' Incentives Are Aligned More Closely With Consumers' Interests

- **Mortgage Bankers, Like Borrowers, Benefit Financially from Positive Loan Performance and Lose from Negative Performance**

Mortgage bankers know at loan origination that their own financial success can depend on the long-term success of the loans they originate. As discussed, mortgage banking involves a variety of financial risks. Economic loss in mortgage lending can be a function of many factors, but usually involves the risk of default (e.g., non-payment of the loan by the borrower). If a loan defaults, a mortgage banker's financial exposure can be considerable whether a mortgage banker holds a loan in portfolio or has sold the loan to a secondary market investor.

In addition to losing the cash flows that come from a performing loan (i.e., servicing fee income and interest payments), when a borrower defaults, the mortgage banker can end up owning the home and incurring the costs associated with maintaining and ultimately selling the house.[22]

22 A 2003 Federal Reserve study estimated that losses on foreclosures range from 30 percent to 60 percent of the outstanding loan balances "because of legal fees, foregone interest, and property expenses." Karen M. Pence, *Foreclosing on Opportunity: State Laws and Mortgage Credit*, (Board of Governors of the Federal Reserve System) (May 13, 2003) at 1.

Additionally, mortgage bankers that also offer other financial services have a significant financial stake in maintaining strong, ongoing relationships with their consumers. Business success for these mortgage bankers relies on their customers' long-term financial success.

■ Mortgage Brokers' Financial Incentives Are Not Linked to Loan Performance

On top of the compensation they receive for sourcing a loan and providing application-related services, mortgage brokers do not receive compensation based on loan performance. Furthermore, brokers do not generally have loan repurchase obligations.[23] As a result, a broker has a strong incentive to close loans and maximize their direct and indirect upfront fees.

While the market for brokerage services and the availability of competition can serve as brakes on broker fees, as indicated, many borrowers do not shop among competing brokers, either because the first broker they encounter is perceived to be an independent advisor shopping for them and/or there is limited competition among originators in the borrower's community.

Since YSPs are not well understood and loan performance does not affect compensation, a broker has a strong incentive to seek the most lucrative indirect fees. There is an information imbalance between broker and borrower that works in the broker's favor. Mortgage brokers are aware of the par rates and yield spreads of various loan products and of various mortgage bankers, and this information informs the broker's decision about what loans to offer any given borrower.[24] At the same time, if a borrower delegates comparison shopping to a broker and the broker's indirect compensation is not understood, the borrower is not taking action to educate himself further about other loan options and is unlikely to question a loan product and/or fees unless or until the borrower runs into trouble with the loan.[25]

23 Some mortgage broker agreements provide for the broker to buy-back loans, but mortgage broker accountability under these agreements is limited by (1) the cost and effort required to enforce the obligation; and (2) the limited capital of brokers, which typically would not be sufficient to repurchase loans, even where a legal or contractual obligation exists.

24 See Kenneth R. Harney, *Study of Loan Fees Shows All Borrowers Not Equal*, The Washington Post (July 19, 2003), p. F01 (discussing a study by Susan E. Woodward, Ph.D.).

25 See 73 FR at 1699 (January 9, 2008).

Current Federal Disclosure Requirements Do Not Reduce the Risks of Steering by Brokers

- **Current Broker Disclosures Provide Consumers with Inadequate Information about Broker Compensation and Responsibilities**

Since 1992, RESPA[26] regulations have required mortgage brokers to disclose on the good faith estimate (GFE), which is provided at the time of loan application, and on the HUD-1 Settlement Statement, which is provided at closing, the amount of direct fees from the borrower and the amount of any indirect fees received from the mortgage banker.[27]

Direct fees to mortgage brokers are listed and included in the borrower's total settlement costs. YSPs to brokers are disclosed as a separate number, outside the column of closing costs, designated as "YSP POC" or "Yield Spread Premium Paid Outside of Closing."[28]

Though the amount of the YSP is disclosed to the borrower and it is identified as a Yield Spread Premium, borrowers are not informed of the YSP's calculation and the fact that the borrower generally pays the YSP through a higher interest rate.[29] Additionally, current disclosures do not tell the borrower if the broker is or is not functioning as an agent of the borrower.[30]

Whether or not a broker is involved in a loan transaction, mortgage bankers' costs and fees related to origination — such as origination and underwriting fees, as well as discount points — are disclosed as settlement costs on the GFE and on the HUD-1 Settlement Statement.[31] The RESPA regulations do not require mortgage bankers to disclose payments from the secondary market or loan officer compensation. HUD has not treated these costs as equivalent to mortgage broker compensation. Unlike YSPs to mortgage brokers, secondary market payments, if they occur, are not paid at settlement and are outside RESPA's coverage.[32] These payments would also require imputation where loans are not sold.

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26 12 USC § 2601 et seq.

27 For current mortgage broker fee disclosure rules, see 24 CFR § 3500.7(a) and (c), and Real Estate Settlement Procedures Act (RESPA) Statement of Policy 1999-1 Regarding Lender Payments to Mortgage Brokers, 64 FR 10080, 10085 (March 31, 1999).

28 24 CFR Appendix A, Appendix B.

29 See *Predatory Mortgage Lending Practices: Abusive Uses of Yields Spread Premiums: Hearing Before the Senate Committee on Banking, Housing and Urban Affairs*, 107th Cong. (January 8, 2002) (statement of Prof. Howell E. Jackson, Harvard Law School).

30 This is the case with regard to federal and state mortgage lending laws. The precise nature of a broker's fiduciary duty is a question that several state courts have addressed, including in California, Missouri, and Texas, finding that brokers' had an agency and/or fiduciary relationship with their borrower-customers. Additionally, a few state legislatures have begun examining the issue. See Joya K. Raha and Andrea Lee Negroni, *Mortgage Brokers-What Fiduciary Duties Exist?* Mortgage Banking (October 2007).

31 12 USC § 2604(c), 24 CFR 3500.7(a).

32 24 CFR 3500.5(b)(7). See also 57 FR 49600 (November 2, 1992), 67 FR 49134, 49140 (July 29, 2002), 66 FR 53052, 53053 (October 18, 2001).

Moreover, mortgage bankers sometimes lose money on these sales. HUD has not regarded employees as separate from their employers for other purposes under RESPA.[33] Importantly, mortgage bank loan officers do not function as independent intermediaries, nor do consumers perceive loan officers in the role of an "intermediary" responsible for shopping for the most favorable loan product available.

■ **Regulators Recognize Broker Disclosures Are Weak and Need Improvement**

For almost a decade, HUD has advocated an improved consumer disclosure that would clearly advise the consumer of the compensation the broker receives in the transaction. Most recently, HUD issued proposed changes to the RESPA regulations intended to enable consumers to compare more effectively origination costs and to inform consumers of the connection between the YSP to be paid to the broker and the interest rate.[34]

Separately, the Federal Reserve expressed "concerns that creditor payments to mortgage brokers are not transparent to consumers and are potentially unfair to them,"[35] recently proposed changes to its Truth in Lending rules (Regulation Z) pertaining to broker fees. The goal of the proposal is to "limit the potential for unfairness, deception and abuse in creditor payments to brokers in exchange for higher interest rates while preserving this option for consumers to finance their obligations to brokers."[36]

The proposed regulations prohibit a creditor (including mortgage bankers) from directly or indirectly paying a mortgage broker in connection with a mortgage transaction unless the mortgage broker enters into a written agreement with the consumer, before a fee is paid, spelling out the broker's total compensation for the transaction, including payments from the creditor and consumer, and the payment does not exceed such amount. The agreement would be required to state: (1) the total compensation that the broker will receive and retain from all sources; (2) that the consumer will pay the entire amount of the compensation even if all or part of it is paid by the creditor; (3) that the creditor will increase the borrower's interest rate if the creditor pays part of the compensation; and (4) that creditor payments can influence the broker to offer certain loan products or terms, which may not be in the consumer's interest or that they may be less favorable than can be otherwise be obtained.[37]

The prohibition would not apply if a broker is (1) subject to a state statute or regulation under which a broker may not offer loan products or terms less favorable than the consumer could otherwise obtain

33 In 1992, when HUD amended its RESPA rules to establish the employer-employee exemption under the affiliated business provisions of RESPA, it indicated that it regarded employees as indistinguishable from their own employers for purposes of RESPA's anti-referral fee provisions. See 57 FR 49600 (November 2, 1992).

34 Department of Housing and Urban Development, *RESPA: Proposed Rule to Simplify and Improve the Process of Obtaining Mortgages and Reduce Consumer Settlement Costs,* 73 FR 14030 (March 14, 2008).

35 73 FR at 1698 (January 9, 2008).

36 Ibid., at 1699.

37 73 FR at 1734 (January 9, 2008).

through the same broker assuming the same loan's terms and conditions or (2) where a creditor can demonstrate that the compensation it pays to the broker is not based on the interest rate.[38]

Barriers to Market Entry Also Differ and Are Greater for Mortgage Bankers

■ Entering Mortgage Banking Requires Significant Financial Resources

The barriers to entry and the costs of being in the mortgage banking and brokerage businesses differ significantly. This reflects the fact that a mortgage banker's business of funding loans and managing the corresponding credit and interest rate risk is more operationally complex and involves more ongoing financial exposure and management than a mortgage broker's business of arranging loan originations and related activities.

To participate credibly in the mortgage industry, a mortgage banker must have sources of capital for funding loans, or secure a credit line for loan originations, known as a warehouse line of credit. Moreover, to maintain and renew its license or charter, a mortgage banker must have a specified level of net worth and/or regulatory capital. The continuing (and continuously escalating) operating costs, including costs associated with regulatory compliance, also help to ensure that undercapitalized and uncommitted mortgage bankers have little incentive to enter the industry, and even less ability to continue with success.

Mortgage bankers also must operate in accordance with multiple levels of government and market oversight as well, such as the guidelines and requirements of the secondary market agencies (Fannie Mae, Freddie Mac, and Ginnie Mae), loan insurers and guarantors (the FHA and VA), and other investors (such as banks and investment funds).

Fannie Mae, Freddie Mac, and the Federal Housing Administration (FHA) approve and oversee any mortgage banker who wishes to work with or sell loans to them. This includes minimum net worth requirements ($250,000 for Fannie Mae/Freddie Mac seller-servicer status; $250,000 for FHA approved mortgagees) and pre-approval reviews for financial and operational soundness.[39] Additionally, private investors and mortgage insurance companies routinely conduct audits of the mortgage bankers with whom they work.

38 Ibid.

39 Institutions (including mortgage brokerages) can also seek approval as Fannie Mae or Freddie Mac sellers only. In the case of Fannie Mae, applicants for seller-only status, however, must have a minimum net worth of $1,000,000 and undergo extensive operational and financial reviews covering all aspects of their businesses. Freddie Mac's public materials do not specify a minimum net worth level for "seller only" status.

■ Prospective Mortgage Brokers Face Few Barriers to Entry

Entering the mortgage brokerage business requires fewer resources and less operational capacity. Mortgage brokers face little federal regulation and, as discussed in this paper, are subject to widely varying degrees of state regulation in an environment where state regulators have limited enforcement staff and resources. Mortgage brokers generally are not required to have funding sources or net worth except in nominal amounts, and even the nominal requirements of state laws are inconsistent. FHA requires brokers who wish to offer FHA-insured products to have a minimum net worth of $63,000 and undergo yearly audits.

Mortgage brokers are typically authorized or chartered only by state governments, and they are far less likely than mortgage bankers to be approved (and subject to ongoing audit by) the secondary market agencies or federal government agencies with lending related regulatory functions.

Current Federal and State Regulatory Requirements Differ and Are More Rigorous for Mortgage Bankers

Mortgage bankers are subject to many complex state and federal laws that impose substantial penalties for non-compliance. Whether they are depository or non-depository institutions, federally or state chartered, mortgage bankers are routinely supervised by federal and state regulators and must comply with a vast array of state and federal laws applicable to their lending activities. Federally chartered mortgage bankers are subject to regulatory review and examination by the federal financial regulatory agencies, and other mortgage bankers are subject to regulation and examination by state regulatory agencies. All mortgage bankers are subject to federal loan origination laws, such as RESPA, the Truth in Lending Act (TILA)[40] and HMDA.[41]

Notwithstanding that the mortgage brokerage industry has grown rapidly since mortgage brokers first appeared in the late 1980s, there are far fewer substantive laws regulating mortgage brokers at the state and federal levels. Additionally, the consequences of noncompliance by mortgage brokers are less severe. The number and variety of regulators focused on mortgage broker regulatory compliance is also fewer and these regulators are concentrated at the state level, where constrained state budgets and thin staffing often translate into minimal oversight.

40 The Truth in Lending Act (TILA) is the popular name for Title I of the Consumer Credit Protection Act, 15 USC § 1601 et. seq.

41 12 USC § 2801 et. seq.

■ State Laws

Both mortgage bankers and mortgage brokers are subject to state licensing and registration under a diverse set of state laws. In addition, state mortgage regulatory agencies (typically, banking and financial institutions departments) have adopted a patchwork of administrative rules that apply to various aspects of the mortgage business. These laws and regulations vary from state to state and, in many cases differ in their treatment of mortgage bankers and mortgage brokers. Even in states whose licensing requirements do not differ substantially between mortgage bankers and brokers, the sheer volume of licensed brokers suggests that brokers are not likely to be subject to the same degree of scrutiny and supervision as mortgage bankers.[42]

National policymakers have identified the inconsistency of broker regulation as an area in need of reform. In fact, the March 2008 report of the President's Working Group on Financial Markets (PWG) includes, among several recommendations affecting the mortgage and credit markets, a call for state financial regulators to implement strong nationwide licensing standards for mortgage brokers.[43]

While mortgage banking regulations also vary state to state, mortgage bankers overall are generally subject to state licensing laws that are more rigorous and extensive than those affecting mortgage brokers.[44] Specifically, state licensing laws tend to impose more burdens (financial, experience, reporting and otherwise) on mortgage bankers than on brokers. Additionally mortgage bankers are sometimes subject to multiple licensing laws depending on their loan product offerings. For example, several states have additional licensing laws for mortgage bankers depending on the loan finance charge, principal amount, or other criteria.[45]

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42 For example, in Nevada, mortgage bankers and mortgage brokers must have two years of verifiable experience in mortgage lending, and neither bankers nor brokers are subject to minimum net worth or surety bonding. However, as of August 2007, the Commissioner of Mortgage Lending in the Nevada Department of Business and Industry had oversight of 294 mortgage bankers and 1,029 mortgage brokers. With the same staff to investigate and enforce the statutes involving both bankers and brokers, there is a greater statistical likelihood that a mortgage banker will be examined and regulated than will a Nevada broker.

43 The President's Working Group on Financial Markets, *Policy Statement on Financial Markets Developments,* (March 2008) p. 12 http://www.treas.gov/press/releases/reports/pwgpolicystatemktturmoil_03122008.pdf

44 There are exceptions to this general rule, as described below. For example, the states of Alabama, Montana, Ohio and Texas regulate mortgage brokers under comprehensive licensing statutes, while most mortgage companies (mortgage bankers) are currently exempt from licensing in these four states, or are subject to a lesser degree of state regulation. In Alabama, the Mortgage Brokers Licensing Act, Ala. Code § 5-25-1 et seq., requires mortgage brokers to be licensed, maintain net worth of $25,000, and complete approved education, but mortgage bankers approved under the National Housing Act (FHA lenders) are exempt from licensing in Alabama. Ohio's mortgage broker registration law, Oh. Rev. Code § 1322.01 et seq., requires registration of mortgage brokers but exempts "mortgage bankers." Mortgage bankers include persons and entities that make, service, buy or sell mortgage loans, underwrite loans and are approved by HUD or the VA or one of the secondary market agencies. Texas has supervisory laws for both mortgage bankers (who must register under Tex. Fin. Code Ann. § 157.001 et seq.) and mortgage brokers (who must be licensed under Tex. Fin. Code § 156.001 et seq). The registration process is simplified; the registration of Texas mortgage bankers is primarily designed to facilitate the handling of complaints from the public. The licensing procedure for mortgage brokers, on the other hand, requires each licensed broker to maintain an office in Texas, have a minimum level of experience and/or education, and pass an examination.

45 For example, the Florida Mortgage Brokerage and Lending Act, Fla. Stat. Ann. ch. 494 et seq., requires both mortgage bankers and mortgage brokers to be licensed by the Office of Financial Regulation. This licensing law applies to residential mortgage loans and to loans on commercial property with five or more dwelling units where the borrower is a natural person or the lender is a noninstitutional investor. The Florida Consumer Finance Act, Fla. Stat. Ann. ch. 516, on the other hand, applies only to lenders (not to brokers) of loans of $25,000 or less where the annual interest rate exceeds 18 percent.

Virtually every state requires the registration and licensing of mortgage broker companies, and almost two-thirds require individual broker licensure or registration. However, the requirements are uneven, and in one case — California — any individual licensed as a real estate agent is automatically licensed as a mortgage broker. Some states call for individual brokers to meet various continuing education, examination, and criminal background check requirements, as well as net worth, surety bond, and auditing requirements, while others do not. Mortgage brokers generally are not subject to multiple licensing laws in a single state based on the size or terms of loans they arrange. Also, recently enacted high-cost loan laws targeted at "predatory lending" generally are directed mainly to mortgage bankers, not to brokers.[46]

State laws regarding a broker's obligation to a borrower vary significantly. Some state laws hold that a broker must act as an agent of the borrower. In other states, courts have ruled that agency relationships exist based on the broker's conduct. Other states have concluded there is no agency relationship implied.[47]

Mortgage bankers are subject to a continuous examination schedule by their chartering agencies, their funding sources, loan guaranty and insurance agencies, and investors. Mortgage brokers are typically authorized or chartered only by state financial institution regulators. They generally are not required to have funding sources or net worth except in nominal amounts, and they are unlikely to be subject to ongoing examination or audit.[48]

New York is an illustrative example of the differences in the state qualification and regulation of mortgage bankers and mortgage brokers.[49] Both mortgage bankers and mortgage brokers are subject to licensing by the New York Banking Department, but the approval criteria are quite different, and the extent of supervision of licensees varies significantly.[50]

In New York, a mortgage banker must have a minimum net worth of $250,000 and access to a $1 million line of credit, plus a surety bond that varies with the volume of loans closed in the calendar

46 For example, the Florida Fair Lending Act, Fla. Stat. Ann. § 494.0078, applies principally to mortgage bankers of high-cost mortgage loans and their assignees.

47 For an overview of the state-by-state imposition of fiduciary duties on mortgage brokers, see "Mortgage Brokers — What fiduciary duties exist?" by Andrea Lee Negroni, Esq. in the October 2007 issue of Mortgage Banking Magazine.

48 As indicated above, the general rule is not universal. For example, in Arizona, the experience required to obtain a mortgage broker license is three years (for each individual licensed broker) but for a mortgage banker, only the "responsible" individual must have three years of lending experience. Moreover, mortgage brokers licensed under Arizona law must take and pass an examination to test their competency, but mortgage bankers are not subject to pre-licensing exams.

49 N.Y. Banking Law § 589 et seq.

50 New York Banking Department data indicates that for calendar year 2006, there were 321 New York-licensed mortgage bankers, of which 124 were examined, an examination rate of 38.6 percent. Only 527 of the 2,431 New York-registered mortgage brokers were examined in 2006, an examination rate of 21.6 percent. Thus, in 2006, mortgage bankers were 70 percent more likely to be examined than mortgage brokers. (The statistics for the first nine months of 2007 reflect an examination rate of 15.1 percent for mortgage bankers and 13.3 percent for mortgage brokers, indicating that the examination frequency gap between the two types of licensees was substantially reduced in 2007.) Moreover, the average duration of an examination of a licensed mortgage banker is 10 days, whereas for a mortgage broker, the average duration of an examination is three days, meaning a mortgage banker's examination was more than three times as long as a broker's.

year preceding the license year. The minimum bond is $50,000, while the maximum is $500,000. An applicant for a mortgage banking license must have five years of verifiable experience in the business of making residential mortgage loans or similar lending and credit evaluation experience.[51]

In contrast, a residential mortgage broker in New York is not required to maintain any minimum amount of net worth, not required to maintain a credit line, and its surety bond requirement ranges from $10,000 to $100,000 depending on the number of loan applications taken in the year prior to the license year.[52]

New York's registration requirements for mortgage brokers are much looser, the main requirement being that the Superintendent of Banking find the applicant's financial responsibility and experience "acceptable."[53] This generally means two years of experience, though some applicants — such as real estate brokers and attorneys — are not required to demonstrate any experience at all.[54] Moreover, a mortgage broker may apply for registration on the sole basis of having completed relevant coursework (with no test or other objective evaluation of whether he or she has learned from the coursework). In contrast, an applicant for a mortgage banker license does not have the option to substitute coursework for the required five years of experience.

■ Federal Laws

Mortgage bankers of all types are subject to an array of federal laws governing loan originations, including TILA, RESPA, the Fair Housing Act, the Equal Credit Opportunity Act,[55] and HMDA.

While mortgage brokers are subject to fair lending laws, they are not subject to HMDA's reporting and disclosure requirements. While mortgage brokers are subject to RESPA and TILA to some extent, consumer disclosure obligations under these laws are mainly the responsibility of mortgage bankers.

TILA

The Truth-in-Lending Act (TILA)[56] is designed to promote the informed use of credit by consumers through meaningful disclosure of its costs. Creditors (i.e., mortgage bankers) making residential mortgage loans for personal, family, or household purposes must provide TILA disclosures except where transactions satisfy specific exceptions. TILA disclosures are detailed and mandatory and

51 3 N.Y. Comp. R & Regs. § 410.1.
52 3 N.Y. Comp. R & Regs. § 410.15(a).
53 3 N.Y. Comp. R & Regs. § 410.3.
54 Individual real estate brokers and attorneys are not required to demonstrate any particular experience to engage in the mortgage brokerage business, despite the fact that the qualifications for these occupations and professions do not ordinarily demand specific familiarity with mortgages or consumer credit.
55 15 USC § 1691 et seq.
56 15 USC § 1601 et seq.

failure to make them timely and accurately subjects the creditor to significant penalties and remedies, including the borrower's right to rescind the loan.

The principal TILA disclosures for mortgage transactions include: the amount financed; the prepaid finance charge;[57] the finance charge; the finance charge expressed as an annual percentage rate (APR); the number, amounts, and due dates of payments; the total of payments; any late payment, prepayment or nonpayment provisions; whether a security interest is taken in the transaction; and the creditor's assumption policy. While a broker may furnish the initial TILA disclosure forms to a mortgage applicant, TILA's disclosure requirements fall squarely on creditors or mortgage bankers in covered transactions.

The potential liabilities and penalties associated with TILA violations provide significant incentives for mortgage bankers to comply.[58] Furthermore, market mechanisms (e.g., the salability of covered loans in the secondary market) add another layer of incentives for creditor compliance. An error in calculating any of the key terms in a TILA disclosure has significant consequences for the creditor.[59] A large body of case law attests to the frequency with which borrowers sue mortgage bankers for TILA non-compliance, both perceived and real. Consumers injured by creditor violations may rescind their loans and sue to recover their damages plus penalties, costs and attorneys' fees. Moreover, assignees of creditors may be liable for violations by original creditors.

Unlike mortgage bankers, mortgage brokers have no liability under TILA, although they may deliver TILA disclosures to consumers.[60] A mortgage broker who verbally underestimates loan costs, finance charges, payments or other key elements of a loan in connection with soliciting an application undermines the purposes of TILA, but bears no liability.

RESPA

The Real Estate Settlement Procedures Act (RESPA)[61] mandates disclosure of certain settlement costs to consumers, including direct broker fees and YSPs, and prevents certain fees among settlement service providers which may increase settlement costs.[62] RESPA requires a mortgage banker to provide a good faith estimate (GFE) of settlement charges at the time of mortgage application

57 "Finance charge" is a difficult definition to work with under the law because of the lengthy list of items included and excluded from its calculation.

58 15 U.S.C. § 1640(a).

59 15 U.S.C. § 1601 et. seq. See also Brophy v. Chase Manhattan Mortgage Co., 947 F. Supp. 879 (E.D. Pa. 1996).

60 15 USC §§ 1602(f), 1631(b).

61 12 USC §§ 2601-2617.

62 "It is clear that at the time RESPA was passed, its basic thrust was to enable consumers to understand better the home purchase and settlement process, and, where possible, to bring about a reduction in settlement costs." Paul Barron and Michael A. Berenson, "Federal Regulation of Real Estate and Mortgage Lending," Fourth Edition, § 2:1 (Thomson/West 2003) (hereafter, Barron, "Federal Regulation of Real Estate and Mortgage Lending").

and a statement of costs at settlement. RESPA prohibits kickbacks, referral fees, and unearned fees among settlement service providers for federally related mortgage loans.[63]

Mortgage brokers may provide GFEs as well. As long as the mortgage broker has provided the GFE, the funding mortgage banker is not required to provide an additional GFE, but the funding mortgage banker is responsible for ascertaining that the GFE has been delivered.[64] However, to ensure compliance, lenders customarily provide their own GFEs to borrowers. A mortgage banker that requires the use of affiliated providers for settlement services is obligated to disclose any relationship between itself and the provider(s).[65]

There are no statutory penalties under RESPA for failure to provide RESPA-required disclosures,[66] but various courts have held that the lack of a statutory penalty does not obviate a borrower's right of action for violation of the disclosure rules,[67] so mortgage bankers can be subject to lawsuits for noncompliance with RESPA. More frequently, federal and state regulators enforce mortgage banker compliance with RESPA disclosure requirements. Mortgage bankers must keep HUD-1 settlement statements and all other documentation in connection with loans, including the application. This recordkeeping obligation does not fall on brokers.

The Fair Housing Act and the Equal Credit Opportunity Act (ECOA)

The Fair Housing Act prohibits discrimination both by direct providers of housing (such as landlords and real estate companies) and mortgage bankers and others who provide services in connection with a "residential real estate-related transaction." Both mortgage brokers and mortgage bankers are subject to the Fair Housing Act. Under the Fair Housing Act, it is unlawful for "any person or other entity whose business includes engaging in residential real estate-related transactions to discriminate against any person in making available such a transaction, or in the terms or conditions of such a transaction, because of race, color, religion, sex, handicap, familial status, or national origin."

ECOA prohibits a "creditor" from discriminating against a loan applicant "with respect to any aspect of a credit transaction" and an "arranger" of credit (such as a mortgage broker) from discriminating on the basis of race, color, religion, national origin, sex or marital status, age (provided the applicant has the capacity to contract), "because all or part of the applicant's income derives from any public assistance program," or "because the applicant has in good faith exercised any right under [ECOA]." While both mortgage bankers and mortgage brokers are subject to these laws, consumers

63 The term "federally related mortgage loan" is broadly defined under RESPA. 24 USC § 2602 (1).

64 24 CFR § 3500.7(b).

65 24 CFR § 3500.7(e).

66 RESPA also requires that prospective borrowers be given a Special Information Booklet which describes settlement costs. The receipt of an application for a federally related mortgage loan triggers the obligation to provide the Booklet. Mortgage bankers or mortgage brokers may provide the Special Information Booklet. 24 CFR § 3500.6.

67 Barron, "Federal Regulation of Real Estate and Mortgage Lending," § 2:41.

and regulators are more likely to make claims against mortgage bankers for any discrimination by independent mortgage brokers because mortgage bankers are perceived to have the resources to pay fines and judgments.

Home Mortgage Disclosure Act (HMDA)

Although mortgage bankers and mortgage brokers are subject to the fair lending laws, only mortgage bankers are required to report and disclose data on mortgage lending activities under HMDA and, thus, are subjected to the scrutiny that HMDA brings. HMDA regulations are the responsibility of the Federal Reserve. The Federal Reserve has stated that the three main purposes of HMDA are:

- To provide the public and government officials with information that will help show whether financial institutions are serving the housing needs of the neighborhoods and communities in which they are located;
- To help public officials target public investments to promote private investments in neighborhoods where investment is needed; and
- To provide data that assist in identifying possible discriminatory lending patterns and enforcing antidiscrimination statutes.

HMDA, among other things, requires covered mortgage bankers to collect, report, and publicly disclose detailed data relating to mortgage applications, denials, and loan pricing. These data include loan type and amount; property location and type; the disposition of the application, such as whether it was denied or resulted in an origination; and the applicant's ethnicity, race, sex, and income.

For 2004, the Federal Reserve began requiring mortgage bankers to report pricing data for first-lien loans with an Annual Percentage Rate (APR) equal to or greater than the rate payable on a Treasury security of comparable maturity plus three percent and for subordinate-liens with an APR equal to or greater than the rate on a comparable Treasury security plus 5 percent. In establishing these requirements, the Federal Reserve sought data on lending patterns in the subprime mortgage market.

As a consequence of these HMDA amendments and the availability of pricing data, hundreds of governmental reviews have been initiated concerning loan pricing by mortgage bankers. These reviews include several by the Department of Justice, the Federal Trade Commission (FTC), the Office of the Comptroller of Currency (OCC), the Federal Deposit Insurance Corporation (FDIC) the Federal Reserve, the Office of Thrift Supervision (OTS), and various state attorneys general. These agencies have continued to use HMDA data in support of other fair lending initiatives, including the review of traditional denial disparity issues, redlining, predatory lending, and steering.

Recommendations for Regulatory Improvements

MBA believes that by appropriately recognizing the differences that exist between mortgage bankers and mortgage brokers, legislators and regulators can take important steps toward addressing consumer protection shortcomings in the mortgage process. MBA recommends the following:

Borrowers Should Have Access to Improved and Timely Disclosures Regarding the Services Furnished by Brokers and Compensation for Those Services

Some have proposed broad prohibitions on compensation linked to loan terms without differentiating between mortgage bankers and mortgage brokers. MBA believes that consumers and the market would be better served with clear information on the amount of total broker compensation, its sources and the broker's functions, early in the process. Such information would encourage consumers to comparison shop among brokers just as they currently do among mortgage bankers, help the consumer understand how compensation derived from rate can be used to pay origination charges and other settlement costs, and increase the likelihood that the consumer ends up with the most favorable loan terms. Additionally, clear information on whether the broker is or is not serving as the borrower's agent would similarly inform the consumer's decision about shopping among multiple brokers.

The recent Federal Reserve proposal to require mortgage brokers to enter into a written agreement with the consumer before compensation is paid to a broker is notable. It would require disclosure of the broker's direct and indirect compensation and help borrowers avoid steering. Additionally, HUD's most recent RESPA proposal seeks to improve YSP disclosures to make clear to the consumer the

link between YSP and a higher interest rate. While MBA has concerns with the HUD and Federal Reserve proposals, MBA applauds both HUD's and the Federal Reserve's work in producing them. Additionally, MBA encourages both agencies to work together as they finalize their proposals.

Some have pointed to studies by the Federal Trade Commission (FTC) to refute the position that more information about broker compensation would better equip consumers to comparison shop for mortgages and mortgage providers.[68] The FTC tested various forms of YSP disclosures with consumers and found that the disclosures did not help consumers identify the least costly loans. The FTC staff report also concluded that the YSP disclosures caused a bias against broker sourced loans. While the FTC's findings highlight the challenges in improving consumer mortgage disclosures, they do not address the problem of consumers' often incorrectly placed reliance on brokers as trusted advisors. Nor do the FTC staff conclusions obviate the need to counter steering through improved consumer information about brokers' compensation and legal responsibilities.

Brokers Who Claim to be or Act as Borrowers' Agents Should Be Treated As Agents Under the Law of Principal and Agent

If a broker asserts or acts in a manner that indicates that he or she is shopping for the borrower, the broker should be subject to the duties of agency.[69] This would clarify that a broker is acting on the borrower's behalf and has an obligation to act in the borrower's best interests.

MBA believes that this is best accomplished through a declaration (or disclaimer) of agency relationship by the broker. This clearly would inform a borrower as to whether he should rely on a broker to shop for him. Mere imposition of an undefined standard of fiduciary duty on all mortgage brokers, irrespective of the borrower's wishes, would likely increase liability and costs to both mortgage bankers and borrowers.

All Loan Originators Should Be Registered and Subject to Appropriate, Rigorous Licensing Standards

MBA supports the President's Working Group on Financial Markets' recommendation that mortgage brokers should be held to stronger licensing and enforcement standards. In fact, MBA supports requiring licensing for all individual loan originators — brokers and bankers — except those employed by an institution with a federal charters (current law exempts employees at federally chartered institutions from state licensing laws). Additionally, there should be a nationwide registry

68 James M. Lacko and Janis K. Pappalardo, "The Effect of Mortgage Broker Compensation Disclosures on Consumers and Competition: A Controlled Experiment," Federal Trade Commission Bureau of Economics Staff Report (February 2004).

69 Agency is a fiduciary relationship created by express or implied contract or by law, in which one party (the agent) may act on behalf of another party (the principal) and bind that other party by words or actions, C.J.S. Agency §§ 2, 4-6, 23, 25–27, 33, 38-40, 58.

of mortgage broker and mortgage banker employees who originate loans. All originators, including those employed by federally chartered institutions, should participate in this registry. A nationwide registry would provide a powerful tool for regulators, industry participants, and consumers in tracking unscrupulous actors.

MBA also supports rigorous and appropriate licensing standards for loan originators. Ensuring that loan originators fall under rigorous licensing requirements will ensure that mortgage brokers, as well as mortgage bankers have the competence and professionalism required to serve consumers. Additionally, MBA supports greater appropriations at the state and federal level for enforcement of such requirements.

Brokers Should Have Sufficient Financial Resources to Provide Relief to Borrowers and Mortgage Bankers Where Necessary

Brokers should be required to maintain a minimum level of financial net worth. Currently, FHA requires brokers offering FHA-insured mortgages to have a net worth of at least $63,000, plus $25,000 for each branch office.

MBA supports establishing a nationwide financial net worth requirement for all mortgage brokers consistent with these requirements. A requirement for minimum financial worth would provide greater protection to consumers and mortgage bankers and help brokers meet their repurchase obligations, making brokers more financially accountable.

Brokers, Where Possible, Should Be Sufficiently Bonded

Additional protection for the public can be obtained if surety bonds are required in connection with licensing of mortgage brokers. MBA supports minimum bonding, where available, of $75,000 or an amount equal to 10 percent of the broker's annual loan volume, whichever is higher.

A number of states already require brokers to maintain surety bonds. Fidelity bonding for the employees of mortgage brokers would be an additional protection for consumers who put their trust in a mortgage broker to obtain mortgage financing. Bonds commonly are available from commercial insurers, and obtaining them would not generally create a hardship on brokers.

Aggrieved consumers and mortgage bankers could file claims for economic losses against the bonding companies. Moreover, since bonding in many cases requires a financial audit, such an audit can provide additional protection to the public and is consistent with existing FHA regulations.

Mortgage Brokers, as Independent Entities, Should Not Be Made Agents of Mortgage Bankers as a Matter of Law

The foregoing recommendations will solve key regulatory concerns in a more targeted manner. Recently, however, one federal legislative proposal suggested that mortgage bankers should be liable for the acts, omissions, and representations made by mortgage brokers whenever they sell or deliver a subprime mortgage to a mortgage banker or for any loan where a mortgage broker receives a YSP from a mortgage banker.

MBA strongly believes this proposal would have deleterious, albeit unintended, effects. Mortgage brokers are independent entities and act independently from mortgage bankers during the loan sourcing and application process. Mortgage bankers lack the ability to control and oversee broker conduct. Making mortgage bankers liable for mortgage brokers, considering brokers' independence, would result in fewer purchases of mortgage broker loans by mortgage bankers. This would decrease competition and lessen choices to borrowers, ultimately increasing borrowers' costs.

Conclusion

The U.S. mortgage market offers a wide array of mortgage credit options and has been a critical factor in increasing national homeownership rates, which are near record levels. Nonetheless, a rising foreclosure rate and recent excesses in the subprime market have brought calls for greater regulation of all aspects of the mortgage process, including the duties and responsibilities of mortgage brokers. The current challenges that the housing market and some homeowners face point to weaknesses in the quality of consumer information and required disclosures.

Both mortgage bankers and mortgage brokers perform beneficial functions in the mortgage market and have been able to offer borrowers an array of credit choices. As this paper illustrates, although complementary, mortgage bankers and mortgage brokers have fundamentally distinct functions and responsibilities. MBA, therefore, urges legislators and regulators to resist pressure to embrace an unwarranted one-size-fits-all regulatory approach. Instead, MBA believes the differences between the brokerage and lending industries should be recognized, considered, and carefully addressed to assure that regulatory inadequacies are properly addressed, consumers are protected, and that the market functions fully and fairly for the benefit of all.

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Summary of the RESPA Statute and HUD's 2008 Proposed RESPA Rule

The RESPA Statute

RESPA was enacted in 1974, for the stated purpose of effecting "certain changes in the settlement process for residential real estate that will result –

(1) in more effective advance disclosure to home buyers and sellers of settlement costs;

(2) in the elimination of kickbacks or referral fees that tend to increase unnecessarily the costs of certain settlement services;

(3) in a reduction in the amounts home buyers are required to place in escrow accounts established to insure the payment of real estate taxes and insurance; and

(4) in significant reform and modernization of local recordkeeping of land title information."[1]

Section 4(a) of RESPA[2] requires the HUD Secretary to develop and prescribe "a standard form for the statement of settlement costs which shall be used... as the standard real estate settlement form in all transactions in the United States which involve "federally related mortgage loans." The law further requires that the form "conspicuously and clearly itemize all charges imposed upon the borrower and all charges imposed upon the seller in connection with the settlement..."[3]

Section 5 of RESPA[4] requires the HUD Secretary to prescribe a Special Information Booklet for borrowers. Sections 5(c) and 5(d) of RESPA require each lender to provide a Good Faith Estimate (GFE), as prescribed by the Secretary, within three days of loan application, and that the GFE state "the amount or range of charges for specific settlement services the borrower is likely to incur in connection with the settlement..."

Section 8(a) of RESPA[5] prohibits persons from giving and from accepting "any fee, kickback, or thing of value pursuant to any agreement or understanding, oral or otherwise, that [real estate settlement service business] shall be referred to any person."[6]

Section 8(b) of RESPA prohibits persons from giving and from accepting "any portion, split, or percentage of any charge made or received for the rendering of a real estate settlement service in connection with a transaction involving a federally related mortgage loan other than for services actually performed."[7]

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[1] 12 U.S.C. §2601(b).
[2] 12 U.S.C. §2603(a).
[3] Ibid.
[4] 12 U.S.C. §2604.
[5] 12 U.S.C. §2607(a).
[6] Ibid.
[7] 12 U.S.C. §2607(b).

Section 8(c) provides, in part, that "[n]othing in [Section 8] shall be construed as prohibiting... the payment to any person of a *bona fide* salary or compensation or other payment for goods or facilities actually furnished or for services actually performed..."

Section 8(c) provides "Nothing in this section shall be construed as prohibiting... (4) affiliated business arrangements so long as (A) a disclosure is made of the existence of such an arrangement to the person being referred and, in connection with such referral, such person is provided a written estimate of the charge or range of charges generally made by the provider to which the person is referred... (B) such person is not required to use any particular provider of settlement services, and (C) the only thing of value that is received from the arrangement, other than the payments permitted under this subsection, is a return on the ownership interest or franchise relationship, or (5) such other payments or classes of payments or other transfers as are specified in regulations prescribed by the Secretary, after consultation with the Attorney General, the Secretary of Veterans Affairs, the Federal Home Loan Bank Board, the Federal Deposit Insurance Corporation, the Board of Governors of the Federal Reserve System, and the Secretary of Agriculture...."[8]

Section 19 of RESPA (12 U.S.C. 2617), among other provisions, authorizes the Secretary to seek to achieve the purposes of RESPA by prescribing regulations, making interpretations, and granting reasonable exemptions for classes of transactions.

HUD's RESPA regulations, Regulation X,[9] implement the statute including the requirements for the GFE to be provided at or within three days of application, the settlement information booklet and the HUD-1 Settlement Statement (the HUD-1) as well as the anti-kickback and affiliated business provisions.

HUD's 2008 Proposed RESPA Rule

The proposed rule would: (1) establish a four-page standard Good Faith Estimate (GFE) form; (2) impose tolerances to limit increases in GFE estimates at closing; (3) revise requirements for disclosure of mortgage broker fees as 'the charge or credit for the interest rate chosen;" (4) make changes to the HUD-1 to facilitate comparison between GFE and HUD-1 charges; (5) establish a new script to be read to borrowers at settlement concerning final loan terms and settlement costs; (6) revise regulations to permit certain average-cost pricing and volume discounts; (7) clarify "required use" requirements to restrict disincentives to use of non-affiliates; and (8) make technical amendments to the RESPA rules. The proposal also announces that HUD will seek legislative proposals to increase enforcement authority, including injunctive authority, under RESPA concerning the GFE and HUD-1, servicing, section 8, title insurance and escrow accounts. The proposal currently would invite public comment for 60 days from the date of Federal Register publication. These proposals are described in greater detail in the below and would:

1. **Good Faith Estimate** – Establish and require the use of a new *standard* GFE form that would disclose: (1) in summary form, the loan details including the loan amount, term, interest rate, initial

[8] 12 U.S.C. §2607(c)(2).
[9] 24 C.F.R. §3500.

payment, rate lock period, whether the amounts for principal, interest and mortgage insurance can increase during the mortgage, whether the loan has a prepayment penalty, a balloon payment and whether the loan includes a monthly escrow payment for taxes and insurance; (2) the costs in ten cost categories including (a) lender and mortgage broker charges known as "our service charge;" (b) the YSP or points as "credit or charge for the interest rate chosen," and then "adjusted origination charges," (c) required services selected by the originator; (d) title services and title insurance; (e) required services the borrower can shop for; (f) government recording and transfer charges; (g) reserves or escrow; (h) daily interest charges; (i) homeowner's insurance; and (j) optional owner's title insurance; (3) Advise the borrower of the relationship between the interest rate and the borrower's settlement costs; and (4) other information for borrowers including how to apply for the loan, using the included shopping chart, estimated taxes, and flood and property insurance premiums.

2. **Application –** Establish accompanying regulations for a new "GFE application" to elicit a GFE which includes name, social security number, property address, gross monthly income and borrower information on the house price or property value; allows a loan originator at its option to charge a fee for providing the GFE; and requires that settlement costs offered in the GFE be open for 10 days.

3. **Tolerances –** Provide, absent unforeseeable circumstances, that the following charges could not increase at settlement from the GFE: (1) loan originators' charges, characterized as "our service charge;" (2) mortgage broker fees, characterized as the "charge or credit for the interest rate chosen "after the borrower locks their interest rate; (3) "adjusted origination charges," also once the rate is locked; and (4) government recording and transfer charges. Would prohibit the sum of other settlement services subject to tolerances, including those that are selected or suggested by the originator and owner's optional title insurance, from increasing by more than 10 percent overall at settlement, absent unforeseeable circumstances. Unforeseeable circumstances include acts of God and other circumstances that could not be reasonably foreseen when GFE was given such as a change to the property price or environmental problems. Where an originator cannot perform or meet the tolerances because of unforeseeable circumstances, originator must document the costs occasioned by them and charge the borrower only the increased costs caused by such circumstances. Also, not bound by tolerances if borrower requests a change in the loan but originator must provide new GFE. If originator offers borrower a new loan, the originator must provide a new GFE subject to new tolerances. Notify the borrower within one day of a decision to reject the loan in final underwriting.

4. **Disclosure of Mortgage Broker Fees –** Require mortgage brokers to disclose all fees from the borrowers and the lender in block 1 as "our service charge," in block 2 disclose a YSP as any credit "for the interest rate of ___%" and subtract it from the "service charge" to arrive at the "adjusted origination charge." Lender must disclose all fees received from borrowers in block 1 and, while lender need not disclose any "charge or credit for the interest rate chosen," lender must check a box on the form indicating that the credit or charge is "included in the service charge.' Also, any discount points must be included in block 2 and added to the "service charge" to arrive at the "adjusted origination charge." Under the rule, HUD also proposes to remove the specific limits on origination charges for Federal Housing Administration loans.

5. **GFE HUD-1 Comparison –** Modify current HUD-1/1A and includes references to corresponding blocks on the GFE. Accompanying rules clarify which services must be separately itemized,

generally including services of third parties but not those of the loan originator or third parties employed by them. Some title services are to be separately itemized.

6. **New Script for Closing Use –** Establish a new script that the settlement agent would be required to read and provide to the borrower at settlement that: compares the loan terms and settlement charges estimated on the GFE with those on the HUD-1; advises whether or not the tolerances have been met; and states the loan terms as contained in the mortgage note and related settlement information.

7. **Average Cost Pricing and Negotiated Discounts –** Permit disclosure of average cost prices on the HUD-1 in accordance with specified computation methods. Also, amends HUD's rules to allow settlement service providers to negotiate discounts in the price of settlement services as long as borrowers are not charged more than the discounted prices.

8. **Revisions to Prohibition Against Requiring the Use of Affiliates –** Change the definition of "required use" so an economic disincentive that a consumer can only avoid by purchasing a settlement service from an affiliated provider would be as problematic under RESPA as an incentive contingent on a consumer's choice of a particular provider. Proposal indicates that it is at least in part directed to homebuilder affiliates but covers other affiliate situations.

9. **Technical Amendments –** Conform RESPA's mortgage transfer of servicing rules to statutory changes and explicitly recognizes the applicability of the Electronic Signatures in Global and National Commerce Act (ESIGN Act)[10] to RESPA disclosures.

10. **Enforcement –** Provide that charging a fee in excess of tolerances or other failures to follow GFE requirements constitutes a violation of Section 5 of RESPA. Solicits comments about whether the industry should have a period of time to remedy an overcharge without violating this provision.

Future Legislation - In its proposal, HUD also announced that it intends to seek legislative changes to: (1) authorize the Secretary to impose civil money penalties for violations of Section 4 of RESPA (the Settlement Statement), Section 5 (the GFE and Special Information Booklet), Section 6 (servicing), Section 8 (kickbacks, referral fees and unearned fees), Section 9 (title insurance), and Section 10 (escrows); (2) require delivery of the HUD-1 to the borrower three days prior to closing; and (3) expand and make uniform the statute of limitations applicable to governmental and private actions under RESPA.

[10] On June 30, 2000, Congress enacted the ESIGN Act (15 U.S.C. §7001-7031) to facilitate the use of electronic records and signatures in interstate and foreign commerce by ensuring the validity and legal effect of contracts entered into electronically. Careful to preserve the underlying consumer protection laws governing consumers' rights to receive certain information in writing, Congress imposed special requirements on businesses that want to use electronic records or signatures in consumer transactions. Section 101(c)(1)(C)(ii) of the Act requires businesses to obtain from consumers electronic consent or confirmation to receive information electronically that a law requires to be in writing. The Act went into effect in October 2000.

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HEARING BEFORE THE

U.S. HOUSE OF REPRESENTATIVES COMMITTEE ON FINANCIAL SERVICES SUBCOMMITTEE ON OVERSIGHT & INVESTIGATIONS

ENTITLED

HUD'S PROPOSED RESPA RULE

WRITTEN TESTIMONY OF

T. ANTHONY LINDSEY

ON BEHALF OF THE

NATIONAL ASSOCIATION OF REALTORS®

SEPTEMBER 16, 2008

INTRODUCTION

On behalf of 1.2 million members of the National Association of REALTORS® (NAR), I am pleased to provide comments to the United States House of Representatives Committee on Financial Services Subcommittee on Oversight and Investigations concerning the proposed rule[1] of the United States Department of Housing and Urban Development (HUD) to amend the Real Estate Settlement Procedures Act (RESPA) Regulation X. The proposed rule is intended to simplify and improve the disclosure requirements for mortgage settlement costs and to protect consumers from unnecessarily high settlement costs by eliminating kickbacks and referral fees.

The National Association of REALTORS® is America's largest trade association, including five commercial real estate institutes and its societies and councils. REALTORS® are involved in all aspects of the residential and commercial real estate industries and belong to one or more of some 1,500 local associations or boards, and 54 state and territory associations of REALTORS®.

REALTORS® have a strong stake in seeing that consumers are provided high value products and services, competitive choices, and simplified disclosures of mortgage settlement costs early in the loan transaction because:

- Real estate agents are typically the first contact in the home buying process, develop close working relationships with clients, and stay with the consumer through settlement. As a result, consumers look to real estate professionals to help them understand the home buying process from beginning to end.
- Abusive lending practices are most likely to occur when consumers are overwhelmed by a transaction laden with unfamiliar financial terms and a confusing array of compensation models and settlement services and cannot shop for competitive rates and high value products and services.
- Early disclosures, clearly presented, will help consumers identify the mortgage product and settlement services which provide the optimal combination of cost and value for their particular circumstances.
- Thorough disclosures that use similar structure and terms in the closing documents will make it easier for consumers and their representatives to identify changes and previously undisclosed charges.

HUD has received nearly 12,000 comment letters on the proposed rule which has now been revised and was sent to the Office of Management and Budget (OMB) for final review on August 21, 2008. OMB has up to ninety days to complete its review of the rule. In light of the fact that HUD utilized only 50 work days to study 12,000 comment letters and revise the proposal, NAR is concerned that some easy "quick fixes" were applied and that there is little likelihood that several critical content and design problems could have been thoughtfully

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[1] 73 Fed. Reg. 14030 (March 14, 2008); Real Estate Settlement Procedures Act (RESPA): Proposed Rule To Simplify and Improve the Process of Obtaining Mortgages and Reduce Consumer Settlement Costs.

considered and resolved in just over two months.[2] NAR's formal comment letter was submitted to HUD on June 12, 2008 and discusses in detail NAR's concerns with the proposed RESPA rule.[3]

The focus of this written testimony will highlight those aspects of the rule that have become, through further study and discussion since the close of the comment period, the major points that NAR believes must be addressed before a final rule is implemented. These points are as follows:

1. HUD's Good Faith Estimate Fails to Achieve Its Objectives
2. HUD's Anti-Competitive Pricing Mechanisms Will Hurt Consumers
3. HUD's Economic Analysis is Flawed

HUD's GOOD FAITH ESTIMATE FAILS TO ACHIEVE ITS OBJECTIVES

The Right Balance Between Simplification and Clear Disclosures Has Not Been Achieved

One of the primary objectives of the RESPA statute is to provide clear disclosures so that homebuyers will better understand settlement costs. NAR supports many of the good intentions HUD has brought to the process, which resulted in an improved appearance of the Good Faith Estimate (GFE) and the translation of complex financial information into language consumers will understand. But HUD has not found the right formula for determining what information to include and how to present it.

This view is widely shared not only by industry, but by other agencies of the government which have called for additional testing and development in order to find the right balance between simplification and disclosure[4]. The calls for additional testing from industry and other federal agencies are based on the unsound testing methodologies employed by HUD. For instance, testing the "closing script" on only ten people in only one round of testing is hardly an appropriate method on which to base an expensive structural change to the settlement service industry.[5] As a result, NAR strongly believes that HUD's proposed disclosure provisions need to be thoroughly tested and improved before they are finalized.

In addition, RESPA directs HUD to regulate disclosures on settlement costs while the Truth in Lending Act (TILA) directs the Federal Reserve Board to regulate disclosures on loan terms. This has resulted in separate disclosures by the two agencies which have proven to be

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2 HUD did not work with industry or announce its changes to the proposed rule prior to submitting it to OMB. Consumers would be better served, and an improved final rule would result, if a comment period was provided for stakeholders to review changes made by HUD to the proposed rule prior to sending the final version to OMB.

3 NAR's comment letter is available at http://www.realtor.org/GAPublic.nsf/files/Letter_HUD_RESPA_GFE_06112008.pdf

4 See Attachment 3: excerpts from comment letters received by HUD calling for additional testing and coordination of disclosures from the Board of Governors of the Federal Reserve, Federal Deposit Insurance Corporation, Federal Trade Commission and the Small Business Administration Office of Advocacy.

5 See p. 145, Summary Report, Consumer Testing of the Good Faith Estimate Form (GFE), U.S. Department of Housing and Urban Development, Office of Policy Development and Research, February 2008.

uncoordinated, overlapping and inconsistent. As a result, the two sets of disclosures emanating from the Federal Reserve Board and HUD are confusing to consumers. This problem has been recognized by Congress since 1996 when it first requested the Federal Reserve Board and HUD to engage in joint rulemaking under TILA and RESPA to harmonize the two sets of disclosures. To date, the two agencies have not undertaken this common-sense task despite repeated requests from Congress and with the knowledge that the existing set of separate disclosures is a primary cause of consumer confusion.

It is critical that HUD work with the Federal Reserve Board to harmonize RESPA disclosures with required Truth-In-Lending Act (TILA) disclosures. Harmonization is necessary to make sure the consumer is not confused by two different sets of disclosures which cover some of the same information and which could be interpreted as being inconsistent with one another.

NAR believes that the current proposal could have been greatly improved if HUD had collaborated with industry and consumer groups – as well as the other federal banking agencies - during the past three years since HUD's RESPA Roundtables in the summer of 2005. Unfortunately, HUD chose not to do so. Instead, it added new provisions never before seen by consumers or industry, rolled them into a complex 96-page regulation and then cut in half a Congressional request to extend the comment period. NAR believes that HUD must take the time required to simplify, coordinate and properly test the new disclosure provisions and include stakeholders in the process if it is to accomplish the goal of better consumer understanding of mortgage and settlement costs.

The GFE is Too Long and its Format Does Not Match the HUD-1

NAR believes the proposed four-page GFE will serve as a psychological barrier to many consumers who will be baffled by four pages of data, fine print and instructions. It is unclear whether consumers will understand (or have the time and inclination to learn) the system proposed for the disclosure of discount points and yield spread premiums (YSP)[6] and the underlying economic incentives that play into these industry compensation models. NAR urges HUD to employ sound testing methodology in conducting further testing on its proposed disclosure models.

NAR also believes it is imperative that the consumer have, at some point, access to <u>all</u> relevant cost information. HUD's decision not to include all costs in its revised GFE will result in consumers getting less than the full disclosure Congress intended in the original statute.[7] While HUD's stated intent in not itemizing all charges is to eliminate junk fees, the result will be just the opposite as the change creates the opportunity to hide additional, undisclosed fees into "packages" to the detriment of consumers.

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6 A recent FTC study recommended that the YSP and "points" not be disclosed they are too confusing to the consumer. (Comments of the Staff of the Bureau of Consumer Protection, the Bureau of Economics, and the Office of Policy Planning of the Federal Trade Commission, April 8, 2008, In the Matter of Request for Comments on Truth in Lending, Proposed Rule, Docket No. R-1305, pp 14-15)

7 "Each lender shall include with the booklet a good faith estimate of the amount or range of charges for ***specific*** settlement services the borrower is likely to incur in connection with the settlement as prescribed by the Secretary." 12 USC 2604(c) *emphasis added.*

Despite the suggestion of its own design consultants and a broad consensus of industry and consumer groups, HUD did not reformat the GFE to match the look of the HUD-1 – a common sense design change that should have been a primary focus of reform. NAR believes this change would greatly assist consumers in understanding whether or not the terms and expenses that were disclosed to them at loan application are those that are the governing terms and costs at closing. It would also obviate the need for the cumbersome and expensive "closing script" that provides information too late in the process to be useful to consumers.

Matching formats for the GFE and HUD-1 statement have been advocated by a number of organizations for some time now. NAR, along with the Center for Responsible Lending, recommended to HUD two years ago that it provide consumers with a one-page summary GFE for shopping purposes, accompanied by a full GFE designed to mirror the format of the HUD-1.

HUD'S CHANGES WILL PROVE ANTI-COMPETITIVE AND WILL HURT CONSUMERS IN THE LONG-RUN

The proposed rule attempts to lower settlement costs through, what in the end is, a government-designed pricing system for closing costs.[8] Provisions on volume discounts and price tolerances, as structured by HUD and embedded in the GFE, will permanently favor large financial institutions but only temporarily benefit consumers. HUD's pricing schemes will reduce competition and promote the concentration of settlement service providers, discourage innovation, reduce the quality of services provided to consumers and ultimately lead to higher closing costs. As we have seen in the ongoing crisis in the mortgage industry, the concentration of economic power in the hands of the privileged few benefits no one.

More specifically, HUD's proposed GFE allows lenders to offer consumers a package of lender-preferred settlement services such as title search, title insurance, appraisals and inspections. The natural consequence of this proposal is that the largest lenders will best be able to apply considerable market pressure on settlement service providers to reduce their prices in order to be included in the lenders'preferred packages. Alternatively, large lenders could price their own in-house or affiliated providers' services below cost simply to acquire market share. While this economic behavior might benefit consumers in the short term, NAR believes that the long-term effect will be to drive small providers out of business followed by an inevitable rise in closing costs once competitors are eliminated.

Consider the following scenario:

> Mr. and Mrs. Homebuyer are presented with a lender-preferred package of settlement services from a large mortgage lender. The Homebuyers are told by the lender that it has done the shopping for them by utilizing its size and market influence to extract significant concessions in the form of volume discounts from its preferred providers.

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8 RESPA, which specifically calls for lowering closing costs through the elimination of kickbacks and referral fees was never intended to be rate-setting statute and lacks any language authorizing HUD to impose pricing systems.

> Next, the lender points out to the Homebuyers that the GFE guarantees the lender's prices in its package. It is emphasized that if the Homebuyers still want to look for their own settlement providers, they can do so, but that the lender will not guarantee the prices of the Homebuyers' providers which could double or triple at closing. The lender concludes by informing Mr. and Mrs. Homebuyer that if they want to select their own providers, they'll also have to pay for another GFE.

Under this scenario, many harried borrowers, already mystified by the entire process and the four-page GFE, may easily be talked out of researching additional companies and will accept the lender's argument that they did the shopping for them. The advantages of sticking with the lender and his preferred choices, such as ostensibly reduced settlement costs through volume discounts and elimination of the risk of dramatic price increases at closing will be persuasive. Futhermore, the borrowers won't have to pay for another GFE.

But there will be unwanted costs to this approach. Clearly, larger lenders will be in the best position to negotiate favorable terms from third party service providers compared to smaller mortgage banks and other settlement service providers. Large lenders will also prefer to work with the larger settlement service providers able to handle the volume generated by a large lender and to reduce administrative costs and risk. Small, local firms, unable to reduce prices or unwilling to reduce the quality of services necessitated by steep price concessions, will be left out. As a result, both the mortgage and settlement service industries will move towards more concentration and thus less competition.

In addition to the anti-competitive nature of the proposal, HUD's pricing mechanisms ignore the importance of value and quality services in the real estate transaction. NAR believes most consumers do not shop for settlement services, or any other significant product based on price alone. Many consumers willingly pay more for the kind of enhanced services that ensures the job is done right and in a timely manner. However, when reduced costs are the focus, quality can suffer.

The current mortgage market crisis provides the best evidence needed to demonstrate that quality does matter. A thorough and professional appraisal offers assurance of the value of a property. The quality of a loan officer's review of a credit report can mean a borrower gets a better interest rate and/or the most appropriate loan for their circumstances. The quality of a title report helps ensure that the buyer has unencumbered ownership of the property purchased and that title risks to lenders and other parties in the transaction are minimized. Creating a system promoting the lowest cost providers as HUD has done with its government-directed volume discounts and price tolerances will favor large lenders and will squeeze quality and local experience out of the system to everyone's detriment. When competition is based on price alone, the chance that consumers will receive poor service and take on more risk increases.

The housing market does not need more "drive by" appraisals where the appraiser, in order to save money, doesn't even get out of car to inspect the home. It does not need loan officers who don't truly understand the differences among the array of mortgage products offered or cannot interpret a credit report so as to direct a consumer to the best mortgage for which they qualify. It does not need closing agents who don't know the customs and rules of the area in which they work.

If recent experience has taught us anything, it is that cutting corners in this business has led to shredded family dreams. The mortgages that have been most troublesome for consumers are the cheapest and easiest to close because they include no documents, no income verification and limited appraisals. The proposed rule, with its extra-statutory mechanisms to lower costs, will only encourage the kind of shoddy services that have resulted in so many inappropriate mortgages and the problems we continue to see in the mortgage and housing markets.

While NAR strongly supports HUD's interest in increased competition and lower prices, government's role should be focused on eliminating kickbacks as called for in the statute, and strong enforcement efforts.[9] HUD's attempt to achieve price reductions through manipulating pricing mechanisms is contrary to HUD's statutory charge, artificially distorts market forces, promotes low-quality settlement services that jeopardize the value of the underlying property and faith in the real estate transaction, and is not in homebuyers' best interest.

HUD's ECONOMIC ANALYSIS IS FLAWED

A. The Proposed Good Faith Estimate

Under the proposed rule, a guaranteed GFE will be required *prior* to loan application. While some components of closing costs are predictable, e.g. the origination fee, other components are not. These costs can change from day to day. Lenders will either have to hedge this risk, or issue a new GFE once an application has been received. Either approach will involve costs that are not considered in the HUD's estimates.

The Department states that it "hopes" that the four page GFE form – along with its accompanying guarantees – will be delivered to consumers free of charge. However, even if this occurs, lenders will undoubtedly seek to recoup their additional costs as part of the origination fee. Originators may also incur additional costs from preparing the GFE twice. In the end, such additional costs will almost certainly be passed through to the consumer.

In an economic critique of the proposed rule which points out a large number of shortcomings in HUD's economic analysis, Dr. Anne Schnare concludes, "[i]f, on the other hand, lenders decide to charge for the form, the GFE could actually *decrease* the amount of shopping that occurs– thereby negating the very benefits that the Department is attempting to achieve."[10]

9 HUD has a poor record of responding to industry requests for clarification. See: Small Business Administration's 2007 Fiscal Year National Ombudsman Report to Congress made available August 25, 2008. The report gives HUD a grade of "F" for timeliness of responses (most agencies received grades of "A" or "B"). It is indicative of HUD's non-responsiveness that NAR sought guidance from HUD in July 2007 on series of RESPA compliance questions and received a partial response 13 months later in August 2008 which, for the most part, reiterated previous guidance and deferred responses to the main issues to other more formal means of providing guidance. On the more uncertain issues, therefore, NAR still has not received the requested guidance from HUD.

10 See Attachment 4: "The Estimated Costs of HUD's Proposed RESPA Regulations" by Dr. Anne B. Schnare, June 3, 2008, for an expanded analysis of HUD's proposed rule.

B. The Proposed Closing Script

HUD assumes that reading the closing script will take about 45 minutes of the closing agent's time, which would almost double the amount of time typically required to close a loan. While HUD calculates the cost of this requirement on the settlement agent's part, it makes no attempt to recognize the costs to the other participants at the closing table, including the borrower/buyer and the seller. This oversight could potentially multiply the projected "opportunity costs" by a factor of four or more, raising the projected cost per loan significantly.

The Department also fails to document the alleged benefits that flow from the closing script. By the time the borrower reaches the closing table, it is highly unlikely that he or she will walk away from the transaction unless serious misrepresentations or issues are uncovered. It is more likely that in cases where a variance exists, someone – the buyer, seller or the real estate agents – will reach into their pocket and pay for an excess that was the responsibility of the loan originator.

In addition, the proposal would have the closing agent act as the consumer's representative but without any ability to control the information being explained. Some have argued that the proposed changes would force the closing agent to assume the role of the "RESPA police." Aside from legal questions regarding whether closing agents, other than attorneys, can play such a role, the requirement would expose the closing agent to additional legal and regulatory risk, which would once again increase the cost of closing.

CONCLUSION

HUD's proposed rule doesn't achieve the objective of simplifying the closing process; distorts the market to the detriment of consumers by imposing anti-competitive pricing mechanisms; and underestimates the cost to industry and consumers alike. HUD's proposed rule imposes wholesale changes on the settlement service industry at a time when the troubled housing market can at least afford ill-conceived fundamental changes, inefficiencies, inequities and understated expenses which NAR believes will result[11]. With regard to costs, the proposed rule will require the industry to modify existing software programs, assume additional risks associated with mandated tolerance levels on the GFE, and provide additional services (e.g. closing script) that may be of dubious value to the consumer.

NAR believes in better disclosures of mortgage terms and third party settlement services to help consumers understand the products they are buying. NAR also supports the policy of ensuring a fair and competitive economic system. But we believe that HUD's RESPA reform proposal should be reworked to focus on common sense disclosures, coordinated with the

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11 HUD provided a 590-page economic analysis in support of the proposed rule. NAR's initial analysis indicates that HUD's estimates of costs are underestimated and that secondary negative effects on small businesses were not considered by HUD. The Department admitted that "a new business model is being put in place for the mortgage industry" but dismisses the issue by stating that "It is difficult to provide comments on a market structure that does not yet exist." (pp. 3-87 Economic Analysis). And, while the Department spends hundreds of pages justifying its estimates of consumer benefits, the reality is that any such benefits are extremely difficult to quantify.

Federal Reserve Board's Truth in Lending disclosures, while eliminating volume discount and tolerance provisions which are anti-competitive because they favor large lenders. It is not enough to simply strip out poorly conceived elements such as the closing script. The entire proposal must be reworked with a focus on meeting the statutory obligation of ensuring clear, concise disclosure of settlement costs.

On May 9, 2008, the White House Chief of Staff, Mr. Joshua Bolten, stated in a memorandum sent to the heads of all executive branch agencies:

> The President has emphasized that the American people deserve a regulatory system that ... ensures a fair and competitive economic system .... We need to continue this principled approach to regulation as we sprint to the finish, and resist the historical tendency of administrations to increase regulatory activity in their final months. We must recognize that the burden imposed by new regulations is cumulative and has significant effect on all Americans.... Every regulatory agency and department has a responsibility for continuing to ensure regulations issued in this final year are in the best interests of the American public.

NAR couldn't agree more and we hope that HUD listened carefully to Mr. Bolten's good advice before submitting its final RESPA rule to OMB. NAR urges all stakeholders involved in this effort to put aside the time constraints of the political calendar and focus RESPA reform on well-tested, clear disclosures formatted to provide simple, clear, and relevant information to consumers and without artificial, anti-competitive pricing schemes. We have the ability to do RESPA reform right and consumers cannot afford another regulation carelessly imposed for political reasons.

Thank you for the opportunity to submit NAR's comments on the proposed rule to address improving disclosure of mortgage settlement costs.

Attachments:

Attachment 1: NAR Draft Summary Good Faith Estimate
Attachment 2: NAR Draft Full Good Faith Estimate
Attachment 3: Excerpts from agency RESPA comment letters.
Attachment 4: Dr. Anne Schnare's economic analysis of HUD's proposed rule.

Attachment 1: NAR Draft Summary Good Faith Estimate

Summary of Guaranteed Good Faith Estimate (Discussion Draft)

Name & Address of Borrower:	Name & Address of Lender or Originating Company:
Property Location:	Date:

LOAN TERMS	
Interest rate: fixed ☐ adjustable ☐	%
If adjustable, maximum yearly increase and maximum total increase	% %
Loan Amount	$
Principal and Interest Estimated Taxes Estimated Insurance	$ $ $
Total Estimated Monthly Payment	$
If adjustable, maximum yearly increase and maximum total increase	$ $
Loan Duration	years
If loan does not fully pay off, amount still owed when loan ends	$
Prepayment penalty: ☐ yes ☐ no	
How computed:	
Maximum amount:	$

SETTLEMENT CHARGES - Summary of Attached Good Faith Estimate "Series" numbers correspond to line designations on the Good Faith Estimate and the HUD – 1 Settlement Form	
Series 800 - Lender Fees: (Origination fee, discount fees, etc.)	$
Series 800 - Mortgage Broker Fee	$
Series 800 - Fees in Connection With Loan: (Appraisal, Credit Report, Etc)	$
Series 900 - Required Advance Payments: (Advance interest, insurance, etc.)	$
Series 1000 - Reserves (Escrow) Required at Closing: (Property insurance and taxes, etc.)	$
Series 1100 - Title Charges (Title search, title insurance, attorney fees, etc.)	$
Series 1200 - Government Fees (Recording fees, taxes, etc.)	$
Series 1300 - Additional Settlement Charges (Survey, pest inspection, warranty, etc.)	$
TOTAL SETTLEMENT COSTS – Cash Required at Closing:	$

Attachment 2: NAR Draft Full Good Faith Estimate

Guaranteed Good Faith Estimate (Discussion Draft)

Name & Address of Borrower:	Name & Address of Seller:	Name & Address of Lender or Originating Co.

Property Location:	Settlement Agent:	
	Place of Settlement:	Settlement Date:

Total Loan Amount: **Interest Rate:** **Term:**

Settlement Charges

801. <u>Origination Fee</u>: These are lender fees to cover the administrative costs in processing the loan. They are often expressed as a percentage of the loan and can vary among lenders.
802. <u>Loan Discount</u>: Points or discount points are a one-time fee by the lender or broker to pay for a particular interest rate. Each "point" is equal to one percent of the mortgage amount.

<u>Other Items Payable in Connection with the Loan:</u> These are fees that the lender charges to process, approve and make the mortgage loan.

Series 800 fees are guaranteed for 30 days from date this document is signed.			Paid by Borrower
801. Loan Origination Fee	%	to:	$
802. Loan Discount	%	to:	$
803. Appraisal Fee		to:	$
804. Credit Report		to:	$
805. Lender's Inspection Fee			$
806. Mortgage Insurance Application Fee		to:	$
807. Assumption Fee			$
808. Flood Certification Fee		to:	$
809. Mortgage Broker Fee	%	to:	$
810. Tax Service Fee		to:	$
811. Processing Fee		to:	$
812. Underwriting Fee		to:	$
813. Wire Transfer Fee		to:	$
814.			$

900. <u>Items Required By Lender To Be Paid In Advance:</u> Interest here is assessed from the date of closing to the end of the month. If no date has been set at the time of issuance of this document, an estimate is provided. The actual amount at closing will be the amount of days remaining in the month times the daily rate of interest based upon the rate of the mortgage. Premiums (lines 902-904) represent advance payment for required insurance.

Series 900 Fees are only estimates. If amounts change, a revised document will be issued.				Paid by Borrower
901. Interest from ______	to ______	@$	/day	$
902. Mortgage Insurance Premium for	______	months to	______	$
903. Hazard Insurance Premium for	______	months to	______	$
904. Flood Insurance Premium for	______	months to	______	$
905. VA Funding Fee				$

1000. <u>Reserves Deposited With Lender (Escrow Account Deposits):</u> These fees identify the payment of taxes and/or insurance and other items that must be made at settlement to set up an escrow account. The lender is restricted in the amount that can be collected. The individual item deposits may overstate the amount that can be collected.

Series 1000 Fees are only estimates. If amounts change, a revised document will be issued.			Paid by Borrower
1001. Hazard insurance	______ months	@$ ______ per month	$
1002. Mortgage insurance	______ months	@$ ______ per month	$
1003. City property taxes	______ months	@$ ______ per month	$
1004. County property taxes	______ months	@$ ______ per month	$
1005. Annual assessments	______ months	@$ ______ per month	$
1006.	______ months	@$ ______ per month	$
1007.	______ months	@$ ______ per month	$
1008.	______ months	@$ ______ per month	$

Attachment 2, Page 2: NAR Draft Full Good Faith Estimate

Guaranteed Good Faith Estimate (Discussion Draft)

Continued (Page 2)

1100. Title Charges. The following fees are not charged by your lender, but by the title company and/or other providers of title-related services you decide to use. The services identified are either required in connection with the loan or can be expected in your transaction. The estimates shown are based on:

the lender's experience in the community where the property is located, or

estimates provided by [Name of Title Company], a company [ ] affiliated
[ ] not affiliated with the lender.

You are free to shop for these services and are not required to use any particular title company.

Series 1100 Fees are only estimates.		**Paid by Borrower**
1101. Settlement or closing fee	to:	$
1102. Abstract or title search fee	to:	$
1103. Title examination fee	to:	$
1104. Title insurance binder	to:	$
1105. Document preparation fee	to:	$
1106. Notary fees	to:	$
1107. Attorney's fees	to:	$
1108. Title insurance binder	to:	$
1109. Lender's coverage	$	$
1110. Owner's coverage	$	$
1111. Commitment fee	to:	$
1112. Endorsement fee	to:	$
1113. Wire fee	to:	$
1114. Electronic doc. Fee	to	$

1200. Government Recording and Transfer Charges: These fees may be paid by you or by the seller, depending upon your agreement of sale with the seller. The buyer usually pays the fees for legally recording the new deed and mortgage (line 1201). Transfer taxes, which in some localities are collected whenever property changes hands or a mortgage loan is made can be quite large and are set by state and/or local governments. City, county and/or state tax stamps may have to be purchased as well (lines 1202 and 1203).

Series 1200 Fees are only estimates. If amounts change, a revised document will be issued.				**Paid by Borrower**
1201. Recording fees:	Deed $	; Mortgage $	; Releases $	$
1202. City/county tax/stamps:	Deed $	; Mortgage $		$
1203. State tax/stamps:	Deed $	; Mortgage $		$
1204.				$
1205.				$

1300. Additional Settlement Charges:		
1301. Survey	to	$
1302. Pest inspection to	to:	$
1303. Home Warranty Fees	to:	$
1304. Elevation Certificate	to:	$
1305.		$
	Total Costs to Close this Transaction:	**$**

Loan Officer **Date**

Applicant **Date** **Applicant** **Date**

RESPA Comment Letters

Selected Excerpts from Government Agencies

Board of Governors of the Federal Reserve Staff Comments (June 13, 2008)

- Board staff believes that the agencies should continue to pursue ways to harmonize TILA and RESPA consistent with the Congressional mandate. (page 2)
- HUD's proposal, however, departs from the approach of a single, integrated disclosure form with little rationale. (page 2)
- We believe that the inconsistencies and other differences between the proposed GFE and TILA disclosure are likely to confuse consumers and, undermine consumers' ability to make informed shopping decisions and avoid unnecessarily high settlement costs. (page 4)
- It does not appear that HUD's testing focused on how consumers understood the specific terms being disclosed on the revised GFE or whether they understood the multiplicity of terms represented in the different loan choices in the side-by-side comparison. (page 4)
- Additional work is needed to test and develop a better disclosure. (page 5)

Federal Deposit Insurance Corporation (undated)

- We have concerns about the length of the proposed GFE and the fact that it does not contain important information about certain loan costs. (page 1)
- We are concerned about whether the proposed GFE truly provides information that consumers need in an easily understandable format. (page 2)
- Additional information often makes a form less useful because the basic concepts are overlooked, and that items of interest to policy experts often do not convey information that consumers use. (page 2)
- At four pages, the proposed GFE may be too long and provide too much information for it to be understood and appropriately used by consumers. (page 2)
- We are not aware of an appropriate means of evaluating whether overall consumer costs would decline as a result of average cost pricing. (page 4)

Compiled by the National Association of REALTORS®

RESPA Comment Letters

Selected Excerpts from Government Agencies

FTC and Bureau of Consumer Protection Staff Comments (June 11, 2008)

- FTC staff supports the development of a single mortgage disclosure document, rather than separate disclosures under RESPA and TILA, so that consumers shopping for a mortgage loan would not need to consult several different disclosure documents to obtain a fuller picture of the loan terms. (page 3)
- The staff recommends that HUD collaborate with the Board of governors of the Federal Reserve System (Federal Reserve Board) to consolidate and reform federal mortgage disclosures. (page 3)
- [P]roposals may have the unintended consequences of further complicating the already complex mortgage lending process, thus causing more consumer confusion than clarity. (page 3)
- FTC staff encourages HUD to consider whether pricing restrictions on the re-sale of settlement service components and prohibitions on referral fees may inadvertently decrease competition and efficiency in the settlement service market. (page 5)

Small Business Administration Office of Advocacy (June 11, 2008)

- Advocacy is concerned that HUD may have underestimated the costs of the proposal and created a potential uneven playing field for some small entities. Moreover, there may be less costly alternatives that achieve HUD's stated goals. (page 2)
- Advocacy urges HUD to give full consideration to the economic information and alternatives suggested by small entities prior to going forward with the final rule. (page 6)
- We respectfully advise HUD to document the additional costs to small entities and consider harmonizing the GFE with the HUD-1 as well as clarifying the provision on tolerances. (page 6)
- Office of Advocacy supports HUD moving forward without the closing script requirement, the volume discount language, and the YSP classification. (page 6)

The Estimated Costs of HUD's Proposed RESPA Regulations

Prepared for the National Association of Realtors®

By

Ann B. Schnare

June 3, 2008

HUD issued a revised set of RESPA regulations on March 14, 2008, following nearly six years of review. These new regulations attempt to improve upon an earlier HUD proposal, issued in 2002 and subsequently withdrawn due to strong opposition. As before, the primary objectives of HUD's proposal are to promote shopping, bring greater "certainty" to closing costs, and simplify and improve the mortgage origination process. However, while these goals are laudable—and while the Department seems to be moving in the right direction—the new proposal still falls short on many of its stated objectives.

There are numerous operational and legal issues that are associated with the proposed regulations. However, this paper focuses on the regulatory impact analysis (RIA) that is used to justify HUD's proposal, in particular, on its estimates of compliance costs. While the RIA is voluminous and covers a variety of topics, HUD's analysis ultimately comes down to a set of relatively simple calculations that attempt to quantify the relative costs of two key aspects of the proposal:

- the revised Good Faith Estimate (GFE); and
- the addition of a "Closing Script" to the settlement process.

This paper discusses some of the limitations of HUD's analysis, and the sensitivity of its estimates to alternative assumptions regarding the probable outcome of the new regulations.

1.0 Key Aspects of the New RESPA Requirements

By HUD's own admission, its new RESPA requirements will fundamentally change the mortgage industry's business model. The redefined GFE and the inclusion of a closing script will add new procedures and risks to both the loan origination and closing process.

The new GFE will be standardized, have a summary page that captures the major elements of origination and closing costs, and contain three additional pages designed to help consumers evaluate the relative attractiveness of a loan. Among other things, these

additional pages will provide a more detailed breakdown of closing costs, as well as a chart presenting alternatives offering higher (and lower) interest rates coupled with correspondingly lower (and higher) up-front costs. In redesigning the GFE, HUD has attempted to give consumers the information that they need to shop for loans and evaluate and compare the different offers they receive.

However, the potential impact of HUD's new regulations extends well beyond the format change embodied in the revised GFE. To begin with, the GFE is currently issued after a borrower has applied for a loan. Under the new regulations, a GFE would be required *prior* to loan application. As noted by HUD, these new regulations will effectively create two types of applications: one for the GFE, another for the actual mortgage. The reason for this new requirement is straightforward: HUD wants consumers to use the GFE to facilitate their shopping process. Presumably, if the regulations have their intended effect, the "typical" consumer would obtain two or more GFEs before actually applying for a loan.

In addition, when a GFE is issued, the originator (defined as the lender or the mortgage broker) will now be required to guarantee the origination fee and certain third party closing costs (e.g., title insurance, appraisal, etc.) for a minimum of 10 business days (subject to certain tolerance levels.) The originator must also specify an interest rate and a lock-in period for the rate, although the originator is free to choose the length of the lock-in period. Once the borrower has accepted the offer and locked-in the interest rate, the terms identified on the GFE would generally be guaranteed until the loan is closed. While HUD has allowed for some discrepancies in the event of "unforeseen circumstances" (e.g., Acts of God, need for a second appraisal, etc.), changes resulting from movements in interest rates or other economic developments are specifically not allowed.

HUD acknowledges that certain information on the borrower will be required in order to guarantee the GFE. As a result, the new regulations will allow the loan originator to collect basic information on the applicant (i.e., name, social security number, property

address, estimated value of the property, and loan amount) before issuing a GFE. If a preliminary review of the data suggests that the borrower would not be qualified for the requested loan, the originator can either reject the application or issue a new GFE for an alternative product. In either event, the originator must keep a record that documents why the decision was made.

Thus, the new GFE requirement will effectively create two distinctly different underwriting processes corresponding to each application type: an initial underwrite for any consumer who requests a GFE based on the limited data provided in the GFE application (i.e., credit score, stated income, loan amount, and estimated property value or sales price); and a second, more comprehensive underwrite for the subset of consumers who ultimately apply for the loan based on more extensive information collected and validated as part of the traditional underwriting process. If consumers use the GFE as a shopping tool, loan originators will have to conduct initial underwrites on large numbers of consumers who end up going elsewhere or not getting a mortgage at all.

Finally, to help ensure that consumers understand the terms of their mortgages and that closing costs do not exceed the thresholds identified in the GFE, HUD has added a new "closing script" to be read to the borrower at the settlement table. The script would contain detailed information about the terms and conditions of the mortgage. It would also include a chart that compares the "firm" costs contained in the GFE to their corresponding line items in the HUD-1 form. While HUD believes that such a comparison will prevent instances of "bait and switch", the Department does not establish a process for resolving any discrepancies that are uncovered at closing, or to otherwise enforce the "guaranteed" nature of the GFE.

2.0 The Potential Impact of HUD's Proposal

As noted earlier, HUD's Regulatory Impact Analysis is voluminous. An extensive review of the document would be impractical within the designated comment period (and probably not particularly productive.) However, a closer look at some of the assumptions

that underlie the Department's estimates suggests that HUD has greatly underestimated the costs of the implementing its new requirements.

The Department estimates that revised RESPA regulations would save the average consumer about $660 in up-front loan origination and closing fees by facilitating and improving the shopping process. It also estimates that the annual compliance cost of producing these savings would be about $100 per loan—$45 for the revised GFE and another $54 for the closing script. Finally, HUD estimates that its proposal would produce efficiency gains of about $86 per loan for borrowers and about $112 per loan for originators due to a reduction in total time spent shopping (or dealing with shoppers.)"[1]

As described in more detail below, there are a number of reasons to suspect that HUD has significantly under-estimated the cost of implementation. In the end, more realistic assumptions concerning these costs would significantly reduce net savings to consumers.

2.1 Impact on Industry Structure

By HUD's own admission, the new RESPA requirements would fundamentally change the mortgage origination process. However, HUD's analysis completely ignores the proposal's potential impact on the structure of the industry. This "partial equilibrium" approach brings the Department's estimates of costs and benefits into question.

Under HUD's proposal, loan originators (and mortgage brokers) will be asked to guarantee not only their own fees, but the fees of third-party settlement service providers. To manage the resulting risk, originators will inevitably seek out contractual arrangements (and pricing concessions) with one or more service providers. As originators seek to form these arrangements, there will be clear winners and losers

[1]HUD estimates that the average consumer would save about an hour in time spent shopping for a mortgage and settlement service providers. It also asserts that these time savings would be realized by originators and settlement service providers since these entities would spend less time answering questions and "seeking out vulnerable borrowers." However, HUD offers no real justification for these estimates. See US Department of Housing and Urban Development, "RESPA: Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis FR-5180-P-01. Proposed Rule to Improve the Process of Obtaining Mortgages and Reducing Consumer Costs," Office of Policy Development and Research. P. 3-120.

throughout the mortgage and settlement services industries. While HUD seems to imply that the only losers will be inefficient or unscrupulous service providers, most commentators believe that, for a variety of reasons, small originators, brokers and settlement service providers will lose at the expense of larger entities.

For example, if the originator requires the borrower to use one of its own service providers, it would probably want to limit its agreements to firms that can handle relatively a large number of transactions. Smaller service providers, who are more likely to have capacity constraints, would inevitably be disadvantaged. Why would a loan originator choose to identify, negotiate, monitor and track the rates of 15 or 20 smaller companies when the same volume of loans could be handled by one or two larger firms? Even if the originator does not require the borrower to use one of its own service providers, it must provide a list of "acceptable" providers as part of the GFE. Since the originator will still be required to guarantee the rates of these recommended companies, such lists are also likely to be short.

The proposed regulations will also tend to favor larger lenders and brokers. Larger originators are in a better position to negotiate rates and to extract pricing concessions from third party settlement service providers. While this may be good for consumers in the short-term, the increased concentration that would inevitably result could eventually produce the opposite effect. For example, larger originators may use their market power to undercut their competitors, and then subsequently move to higher rates once their competitors have left the market. Regardless of the eventual impact, the number of active players in the market would undoubtedly decline.

While the Department admits that "a new business model is being put in place for the mortgage industry," it makes no attempt to take these secondary effects into account in estimating the costs and benefits of the proposal. In fact, HUD dismisses the issue by stating that "it is difficult to provide comments on a market structure that does not yet exist."[2] Given the current turmoil in the mortgage market, one wonders if now is the time

[2] HUD, op. cit. p. 3-87.

to implement a new regulation that would result in such structural change. At a minimum, this issue deserves to be given more than cursory attention from HUD before it finalizes its regulation.

2.2 The Cost of the New GFE

The Department also underestimates the costs of implementing the new GFE requirements. Among other things, HUD's proposed regulations will require the industry to modify its existing software programs, train staff on the use of the form, process and track multiple applications from multiple borrowers, underwrite GFE applications for borrowers who end up going to other lenders, and require originators to assume the additional risks and costs that are associated with the mandated tolerance levels on the GFE.

HUD estimates that the annual cost of the expanded GFE will be $44.50 per loan. However, in deriving its estimates, HUD either ignores or dismisses many of the factors noted above. This section highlights some of the major limitations of HUD's analysis, which include:

- understating the total number of GFEs that would need to be issued and tracked;
- ignoring the operational and hedging costs associated with the guarantee; and
- ignoring the costs of the initial underwrite, including the costs of obtaining additional FICO scores.

Accounting for these and other factors would significantly increase the estimated costs of the GFE.

The Number of Good Faith Estimates

HUD assumes that roughly 1.7 GFEs would be produced for every completed mortgage origination. Thus, in order to produce 12.5 million loans (HUD's baseline estimate for a

typical year), HUD assumes that originators would have to issue roughly 21.250 million GFEs (i.e., 1.7 GFEs per loan x 12.5 million loans.) The 1.7 ratio used by HUD is based on the observed relationship between loan applications and loan originations, as reported in HMDA data.[3] (The ratio is significantly higher than 1.0 due to the fallout that occurs when loan applications are either rejected or voluntarily withdrawn.) In effect, using a 1.7 ratio to estimate the number of GFEs that are associated with a given origination volume assumes that the new regulations will not affect the total number of GFEs that are issued in any given year (or, alternatively, that there will be just one GFE per mortgage application.)

However, there are a number of reasons that a higher ratio should be used. Assume, for example, that the revised GFE does not affect the fallout that occurs once a formal application has been received (i.e., that the ratio of mortgage applications to originations remains at 1.7.) Even if the average borrower obtained just two GFEs, the total number of GFEs in a typical year would rise from 21.3 million (HUD's estimate) to about 42.5 million (i.e., 2 GFEs per application x 1.7 applications per loan x 12.5 million loans.) While one could argue that better information on the part of consumers would reduce the number of loans that were rejected or withdrawn after a loan application has been filed, even if the fallout rate were cut in half—a highly unlikely event—the number of GFEs that are issued in a typical year would be 33.75 million, or about 59 percent higher than the estimate used by HUD.[4]

Thus, it seems highly likely that the ratio of GFEs to loan originations that is embedded in HUD's projections (1.7) is far too low. Under the alternative assumptions presented above, the ratio of GFEs to originated loans would more likely range between 2.7 and 3.4 even if one assumes that the average consumers obtains just two GFEs. These higher ratios would translate into proportionally higher compliance costs.

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[3] HUD, op. cit., p. 2-6.

[4] Cutting the fallout rate by half would result in a ratio of 1.35 loan applications for each originated loan. Assuming that each borrower obtains 2 GFEs before a applying for a loan—and that it there are 1.35 applications for every loan—results in 2.7 GSEs per origination.

In deriving its estimates, HUD assumes that the annual costs of the revised GFE primarily relate to processing and tracking the applications.[5] If one assumes that 21.250 million GFEs would be issued in a typical year, average costs per originated loan would be $44.50—the estimate produced by HUD. However, if one assumes that between 34 and 43 million GFEs would be issued, the average annual cost per originated loan would rise to $71 to $89, respectively.

While the ratios that are used to derive these various estimates are admittedly somewhat arbitrary, one thing seems clear: either HUD has seriously under-estimated the number of GFEs that will be issued under its new regulations or the regulations will not produce the amount of shopping behavior that the Department would like to achieve.

The Operational and Hedging Costs of the GFE

As noted above, HUD's estimates of the on-going costs of the GFE are primarily based on the amount of additional time it will take to process the application and produce the revised GFE form. HUD ignores or dismisses the operational and hedging costs that would be associated with this new requirement, including the costs of hedging the interest rate that is offered on the GFE.

Under the proposed regulations, the originator's fee (excluding the YSP) and certain components of closing costs must be guaranteed for at least 10 business days (subject to a 10 percent tolerance level that is applied to the sum of all applicable third-party costs.) However, HUD allows the originator to establish the lock-in period for the interest rate. Until the rate is locked, all interest-related charges, including the yield spread premium, are allowed to float.

Conceivably, the originator could choose a lock-in period that is considerably shorter than the 10 business days required for other components of the GFE in order to minimize

[5] As described in more detail below, HUD either ignores or dismisses the additional underwriting, operational and hedging cost that would be associated with the new guarantees.

its hedging costs. While this would defeat one of the major objectives of HUD's proposal—namely, to fix the mortgage terms for at least 10 business days in order to facilitate the shopping process—HUD does not address this issue in its RIA. Instead, HUD asserts that its decision to reduce the guarantee period from 30 to 10 business days would eliminate any significant operational and hedging costs that were associated with its 2002 proposal.

However, even a relatively short lock-in period for the interest rate on the GFE could add significant costs to the originator over and above the hedging costs that now occur once a formal application has been received. Suppose, for example, that originator set the lock-in period to 10 business days—a move that would certainly make the offer much easier for consumers to understand and would be consistent with HUD's objectives.[6] According to our estimates, the cost of the hedge would be about 4 basis points (i.e., 0.04 percent) of the dollar value of requested loan.[7] If one assumes that 3.7 GFEs are issued for every loan that gets originated, the initial interest lock would cost about 13.6 basis points per loan (i.e., 4 bps per GFE x 3.7 GFEs per origination.) On a $200,000 mortgage, this would add about $272 to the cost of the loan. Even if one uses HUD's assumptions regarding the ratio of GFEs to originations, the average cost of the interest rate hedge would be about $180 per loan (i.e., 4 bps per GFE x 1.7 GFEs per origination.)

Multiple Underwriting

HUD has also not factored in the additional costs of underwriting the GFE. While it notes in its RIA that the originator would be required to update the credit report once a formal loan application has been received[8], it makes no attempt to account for this

[6] HUD's revised GFE has multiple dates for the offer: one for the origination fee and third party settlement costs; one for the quoted interest rate; one for the settlement date; and one for the number of days that the loan must lock before closing. The multiplicity of dates could well lead to borrower confusion.
[7] The value of the hedge can be estimated by comparing differences in the rates that Fannie Mae and Freddie Mac are currently being offering for loans with different delivery periods. On May 15th, the interest rate spreads on Fannie Mae and Freddie Mac 30 and 60 day deliveries were about 8 basis points. Guaranteeing the interest offered on the GFE for 10 business days (i.e., 12 to 14 calendar days) would cost about half of this amount, or roughly 4 bps.
[8] HUD, op. cit. p. 3-70.

additional step in its cost analysis. In effect, HUD assumes that the initial screening that would occur when the GFE is issued would simply replace the initial screening that would otherwise occur once a formal application has been received. This argument might make some sense if one accepts HUD's premise that its new regulations will not affect the number of GFEs that are ultimately issued. However, the argument falls apart if one assumes that HUD's regulations will lead to significant increases in the total number of GFEs.

For example, if one assumes that the ratio of GFEs to originations is 2.7 instead of 1.7, loan originators would have to pull at least one additional credit report for every mortgage origination (i.e., 2.7 – 1.7). According to HUD, the average credit report costs about $25.[9] This additional expense would increase the Department's estimated cost of the GFE ($45 per loan) by 56 percent. Furthermore, the additional underwriting step would undoubtedly add to total processing time. If one assumes that preliminary screening will take about 10 minutes to complete, the total cost of the initial underwrite would rise to about $30 per loan—$25 for the initial credit pull and another $5 for the underwriter's time (valued at $31.14 per hour.)[10] If one assumes that the ratio of GFEs to originations is even higher—for example, 3.4—the additional underwriting costs would add about $52 to the cost of a typical loan.

Alternative Estimates of Annual Costs of GFE

Exhibit 1 summarizes how changes in HUD's assumptions could change the estimated cost of the GFE. The columns reflect different assumptions regarding the ratio of GFE applications to loan originations, which affect the number of GFEs that would be issued in a typical year. The first column assumes that the new regulations do not affect the total number of GFEs that are issued (i.e., HUD's assumption) and that the ratio of GFEs to total loans is 1.7. The second and third columns present alternative estimates based on

[9] HUD, op. cit. p. 3-95.
[10] HUD uses different hourly wages to value the originator's time. In its estimates of efficiency gains, HUD values the time saved by originators at $72 per hour. However, in its estimates of GFE costs, it uses $31.14 per hour. To be conservative, we use the lower figure here.

ratios of 2.7 and 3.4, respectively.[11] As described in an earlier section, such higher ratios are not unreasonable, particularly if consumers actually use the GFE to assist them in their shopping process.

Exhibit 1: Estimated Annual Cost of the GSE per Loan

	Number of GFEs Per Originated Loan		
	1.7	**2.7**	**3.4**
Processing Costs	$ 45	$ 71	$ 89
Hedging Costs[12]	$136	$216	$272
Initial Underwrite[13]	0	$ 30	$ 52
Added Cost per Loan	$181	$317	$413

As illustrated by the chart, accounting for hedging and underwriting costs, and applying more realistic assumptions regarding the expected number of GFEs, would have a dramatic impact on the estimated costs of the GFE. Instead of the $45 estimated by HUD—the number presented in the upper left hand cell of the chart—projected costs could easily range from about $300 to $400 a loan. Moreover, even these higher estimates may be conservative. For example, they do not include any legal costs associated with the litigation risk that would inevitably arise from a "guaranteed" GFE.

[11]The 2.7 ratio assumes that the average consumer obtains 2 GFEs and that the fallout rate from application to origination is reduced by half (i.e., to 1.35). The 3.4 ratio assumes that the average consumer obtains 2 GFEs and that the ratio of applications to originations remains the same (i.e., 1.7).

[12] Assumes that the interest rate offered on the GFE is good for 10 business days and that the average loan amount is $200,000.

[13]The estimates assume that an applicant's credit report is pulled only once, when the GFE is approved. This may be unrealistic given the time that could elapse between GFE and loan application. Costs would be higher if one assumes that credit scores would have to be pulled again when the borrower actually applies for a loan.

2.0 The Costs of the Closing Script

HUD also underestimates the cost of the proposed closing script, which would provide little, if any value to the consumer. By the time the consumer comes to closing, it is far too late to change the terms of the loan. And if discrepancies in closing costs are found, there is no established process to resolve such issues or to enforce the guarantees established by the GFE.

Implementation issues aside, HUD assumes that preparing and delivering the closing script will take about 45 minutes of the closing agent's time, which would double the amount of time typically required to close a loan. HUD estimates that this additional step would add about $54 to the cost of the loan, or about $1.20 for each additional minute that the title agent spends in preparing and delivering the closing statement.

While HUD calculates the cost of this requirement on the settlement agent's part, it either dismisses or ignores the costs to the other participants at the closing table, including the borrower, the borrower's spouse, the real estate agent, and in some states, two or three attorneys. HUD claims that its requirement will impose no additional costs on borrowers, since they would otherwise be left on their own to review and compare the GFE to the fees recorded on the HUD-1 form. However, even if one accepts this premise, there are likely to be additional professionals at the closing table who will have to sit through a longer settlement process.

HUD estimates that it will take about 15 minutes to read the closing script and answer any questions. Assuming that the opportunity costs for everyone present would be about the same as the closing agent's time, the cost of the closing script would rise by about $18 for each additional person involved. For example, if one assumes that three additional people are present at closing, the cost of the closing script would double to $108—$54 for the closing agent's time (45 minutes) and another $54 for the time of the three other attendees combined (3 x 15 minutes, or 45 minutes.)

HUD also fails to recognize the impact that increasing the amount of time at closing would have on other related costs. Most closings occur at or near the end of the month. Roughly doubling the amount of time that it would take to complete the transaction would create additional demands on space to handle the same volume of loans. Yet such additional costs are not considered in the Department's analysis. Nor does the Department consider the legal and regulatory risk that now must be borne by the closing agent. In effect, HUD's proposal would have the closing agent act as the consumer's representative and serve as the "RESPA police." Aside from legal questions regarding whether closing agents other than attorneys can play such a role, the requirement would expose the closing agent to additional legal and regulatory risk, which would once again increase the costs of closing.

The Department also fails to document the benefits that flow from the closing script. By the time the borrower reaches the closing table, it is highly unlikely that he or she will walk away the transaction unless serious misrepresentations or issues are uncovered. For example, according to the Department's estimates, typical charges for title services and other third party fees come to about $1841.[14] Thus, a variance of greater than $184 would cause a potential RESPA violation. Indeed, in two of the examples presented in the Federal Register, differences of $14 to $15 could potentially bring the closing process to a halt.[15] It is highly unlikely that anyone involved in the settlement process would walk away at this point in the process. Someone—either the closing agent or the real estate agent—would undoubtedly reach into their pockets to pay for an excess that was the responsibility of the loan originator.

While HUD has allowed for fees that exceed the tolerance level to be justified and resolved at the closing table, the most likely party to resolve any discrepancies—the loan originator—would typically not be present. If the lender were required to be available by

[14]According to the Urban Institute, total title fees and other third party charges had medians of $1267 and $574, respectively. See Federal Register, Vol. 73, No. 51, March 14, 2008, p. 14106.
[15] In one example, the GFE estimated third party closing costs at $642, while actual costs came in at $715. The difference ($78) exceeded the 10 percent tolerance level by $14 (i.e., $78 - $64.) See Federal Register, op. cit., p. 14079. In another example, third party costs were estimated to be $809, but came in at $905. The difference ($96) exceeded the 10 percent tolerance level by $15 (i.e., $96 - $81.) See Federal Register, op. cit., p. 14091.

phone at the time that the script were read, this would add another $18 to the estimated cost of this provision (assuming that the value of the originator's time was the same as the closing agent's.)

In short, HUD estimates that the closing script would add about $54 to the average cost of a loan. However, more reasonable assumptions would yield costs that are probably at least double this amount.

4.0 Impact on Shopping

The Department states that it "hopes" that the four page GFE form—along with its accompanying guarantees—will be delivered to consumers free of charge. However, even if this occurs, lenders will undoubtedly seek to recoup their additional costs as part of the origination fee. This was the assumption used by HUD in deriving the estimated costs of its proposal; it was also used to derive the alternative estimates presented here.

If, on the other hand, lenders decide to charge for the form, the GFE could actually *decrease* the amount of shopping that occurs—thereby negating the very benefits that the Department is attempting to achieve. Even if one accepts the Department's estimate that the cost of the GFE would be just $45, charging the consumer this amount simply to provide a quote would put a significant damper on the amount of shopping that actually occurs.

5.0 Conclusions

HUD estimates that the on-going costs of its new regulations would be about $100 per loan—$45 for the revised GFE and $54 for the closing script. However, the analysis presented here shows that actual costs are likely to be considerably higher. Even under reasonably conservative assumptions, the average cost of the GFE would be well over $300 per loan, while the cost of the closing script would probably be closer to $100. As a result, a relatively large share of the savings that are envisioned by the Department could easily be absorbed by these higher costs.

It is important to recognize that most of the additional costs described in this report are associated with the guarantee embedded in the revised GFE, as opposed to the form *per se.* The Department should seriously question whether its desire to provide greater certainty in closing costs is worth these additional costs. Presumably, a simplified GFE could produce many of the shopping benefits envisioned by HUD by making the terms of the loan more transparent.

Indeed, an earlier study by HUD concluded that on average, closing costs on the GFE were relatively good predictors of closing costs and were, in fact, slightly higher than those recorded on HUD-1 forms.[16] While the study was based on a small number of observations—and while it found that actual closing costs were significantly higher than those provided by the GFE in an unspecified "minority" of cases—the Department has offered no compelling evidence that "bait and switch" is a widespread phenomenon.

Presumably, HUD could achieve most, if not all of its stated objectives by simplifying and standardizing the GFE without imposing additional costs, complexities and paperwork on a process that is already far too cumbersome. In the end, the simplest solution may be the one most likely to succeed.

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[16] Mark Shroder, "The Value of the Sunshine Cure: The Efficacy of the Real Estate Procedures Act Disclosure Strategy," Cityscape: A Journal of Policy Development and Research, Vol. 9, Number 1, 2007.

Testimony
to the
Subcommittee on Oversight and Investigations
of the
House Committee on Financial Services

regarding

HUD's Proposed RESPA Rule

by

on behalf of the low income clients of the
National Consumer Law Center
and the
National Association of Consumer Advocates

September 16, 2008

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Testimony
on
HUD's RESPA Rule

Chairman Watt, Congressman Miller, Members of the Committee, thank you for inviting me to testify today regarding HUD's proposed RESPA rule. My comments today are provided on behalf of the low income clients of the National Consumer Law Center ("NCLC"), as well as the National Association of Consumer Advocates.

The staff of NCLC applauds HUD for its consistent efforts, over more than a decade, to improve the regulations under RESPA . As you know, this is its second set of proposed regulations, following a series of public and private meetings over many years. HUD has consulted with representatives from the diverse industries RESPA, as well as consumer representatives. We can see the impact of these discussions in the language of the proposal. The issues addressed in the proposed regulations are difficult and complex, and their resolution will affect millions of consumers and industry participants in the home mortgage business.

The latest proposal is a good way down the road toward positive reform of the RESPA regulations. **We do not believe that the current effort should be suspended – just continued.** ***HUD should continue to improve the regulations – as recommended by us – and finalize them.*** These regulations must be improved as recommended in our comprehensive comments before they are finalized.[1]

I have been asked to testify today on a variety of topics:

1. Any changes you believe would be desirable to the proposed RESPA rule.
2. The need for harmonization of HUD's proposed RESPA rule with the TILA rule issued by the Federal Reserve Board.
3. The adequacy of consumer testing regarding the proposed GFE.
4. Whether changes are needed to the Good Faith Estimate (GFE).
5. The potential challenges with implementing the proposed "closing script."
6. The benefits and limitations of the disclosure of yield-spread premiums to consumers.
7. Other needed legislative and regulatory changes to RESPA.

Although I have not been asked what we *like* about the proposed regulations, HUD's proposal includes many positive features which we heartily endorse and which we believe will

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[1] NCLC's comments on the proposed RESPA regulations, were filed on behalf of the low income clients of NCLC, as well as Consumer Action, the Consumer Federation of America, and the National Association of Consumer Advocates. The comments can be found at http://www.consumerlaw.org/issues/predatory_mortgage/content/NCLC-RESPAcomments08.pdf.

improve the transparency of the complex mortgage settlement process. Please refer to our extensive comments on the proposed regulation for a full explanation of these provisions.

The issues I was asked to address are separately answered below.

1. Summary of Recommended Changes to the RESPA Rule.

There are several overarching concerns (and a myriad of important details) that need to be improved to ensure that the Rule does in fact protect consumers, instead of simply providing a shield behind which mortgage originators can hide inappropriate, unfair, and illegal activities. While much of HUD's work on the Good Faith Estimate (GFE) is excellent, as detailed in our comments, several specific provisions must be retooled to prevent harm to consumers. These include:

- Most importantly, the APR must be included instead of the interest rate. The APR is the sole unitary measure of the cost of credit, combining the effect of both rates and fees. Failure to include it on the GFE limits consumers' ability to shop for credit.

- The total of settlement costs should be highlighted, rather than various subtotals. In general, detail on settlement costs should be downplayed. Interest and other loan terms are almost always the largest component of cost; consumers should not be encouraged to focus on settlement costs instead of the combined effect of rate, fees, and term—the APR.

- The HUD-1 should be further synchronized with the GFE.

- The disclosure of mortgage broker fees must be changed. As currently written, the disclosure of mortgage broker fees presumes that borrowers receive a tradeoff between settlement costs and lender payments to brokers. Most available evidence suggests that in most instances, and certainly when both the borrower and the lender pay the broker, that all costs, including interest, fees, total broker compensation, and settlement costs, increase. HUD should not mandate a counterfactual presentation of reality.

- The closing script (or any application script, if required instead), must notify borrowers of the loan's APR and any applicable rescission rights and must omit the acknowledgement.

- The proposals to permit average cost pricing and volume based discounts only if consumers unequivocally benefit require important tweaks in the language of the regulations to ensure that all charges actually imposed on the consumers are always disclosed.

- The prohibition against required use needs amendments to ensure that HUD's intentions are fulfilled.

2. The Need for Harmonization of HUD's Proposed RESPA Rule with the TILA Rule Issued by the Federal Reserve Board.

The revision of the settlement statement, important as it is, must not undermine the enforceability of the Truth in Lending Act ("TILA"). Enforcement of the TILA and the Home Ownership and Equity Protection Act ("HOEPA") depend on full itemization of settlement costs. Remedies for the violation of TILA and HOEPA can include significant statutory damages and the right to rescind the loan, with the result of saving a home from foreclosure. In transactions to which RESPA applies, TILA rules say that the lender need not give an itemization of the amount financed if it provides both the GFE and settlement statement.[2] The itemization of the amount financed is essential for regulators, consumers, and their advocates to determine if TILA's fundamental disclosures – the APR, the finance charge, and the amount financed – were made correctly. Mortgage lenders consistently use the GFE and settlement statement as a replacement for the itemization of the amount financed.

HUD proposes to require lenders to disclose as a lump sum their origination charges and all title services.[3] This is certainly an improvement from the perspective of consumer understanding. However, not all origination services and title services are clearly all-in or all-out of the TILA finance charge. Under the statute, for example, title insurance is excluded from the finance charge.[4] Other charges related to title insurance, including the settlement fee, courier fees, or document preparation fees, may be included in the finance charge, however, particularly if they are not bona fide and reasonable.[5] Similar inconsistencies plague other origination fees.

Effective disclosure of costs requires bundling of all closing costs. However, the Federal Reserve Board has allowed the finance charge to become debundled.[6] As a result, HUD's improvement of disclosure in the settlement context could impede review of lender's compliance with the disclosure requirements of TILA.

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[2] Official Staff Commentary on Regulation Z, § 226.18(c)-4.

[3] 73 Fed. Reg. 14030, 14058 (Mar. 14, 2008).

[4] 15 U.S.C. § 1605(e)(1).

[5] *See generally* National Consumer Law Center, Truth in Lending §§ 3.9.5, 3.9.6 (6th ed. 2007.)

[6] *See, e.g.,* Elizabeth Renuart & Diane E. Thompson, *The Truth, the Whole Truth, and Nothing But the Truth: Fulfilling the Promise of Truth in Lending*, 25 Yale J. on Reg. 181 (2008).

Absent coordination with the Federal Reserve Board on a more useful and expansive definition of the finance charge, and statutory changes to the TILA itself, the final settlement statement must not bundle either all title or origination charges. Consumers should be provided, as HUD proposes, a summary of the charges and a comparison to the total disclosed on the GFE, to facilitate

shopping. Consumers must also, however, be provided the detail in a form they can keep, to permit review for TILA compliance.

The closing script proposed by HUD does not address the TIL disclosures. Its failure to do so undermines the clear and conspicuous disclosure required under TILA. The closing script, in addition to reflecting the contract terms of the note, must reflect the TIL disclosures.

3. The Adequacy of Consumer Testing Regarding the Proposed GFE.

HUD's consumer testing focused exclusively on whether consumers could chose the cheapest loan when the only difference in cost was a change in settlement costs, dependent on how large the lender-paid broker compensation was. Unfortunately, an increase in lender-paid broker compensation often means an increase in both the rate and the total settlement costs. HUD has not tested whether or not consumers can use the loan summary sheet, or the tradeoff box, or any other element of the proposed GFE, to determine which of two loans that vary by more than settlement costs—by interest rate, term, or loan features—is cheaper or otherwise more desirable. What HUD tested was consumer's ability to choose the loan with the lower settlement costs when the two loans are otherwise comparable. Most loans in the market will vary by more than the total settlement costs. Any two loans offered a consumer are likely to vary by the interest rate, the amortization schedule, the term of the loan, whether the rate is fixed or adjustable, and a myriad of other factors, all of which affect the overall price. While the simplified, standardized GFE and the tradeoff table do a good job of aggregating most of that key information, HUD has done no testing to see whether consumers can, on average, using the GFE, determine which of two loans is cheaper or which better fits individual circumstances.

4. The *Major* Changes Needed to the Good Faith Estimate (GFE).

In its proposal, HUD has taken many important steps towards improving market transparency. The standardization of the GFE, increasing the linkages between the GFE and the settlement statement, and mandating the early provision of a binding GFE should increase consumer understanding and competition in the mortgage marketplace. The inclusion of key loan terms, including the maximum payment and the maximum loan balance, is vital information consumers do not currently receive and essential to consumer choice.

In the current marketplace, GFEs – when given – often bear no relationship to the final closing costs. Some originators only provide the GFE at the closing; others give GFEs

that significantly low-ball total costs. The variance in GFE forms, the lack of congruence between GFEs and settlement statements, and the failure to place any of these documents in consumers' hands in a final format before closing all have hindered competition in the mortgage marketplace. HUD's movement to standardization will improve its comparability to the settlement statement. More importantly, by requiring that some of the terms of the GFE be binding, HUD will reduce bait and switch tactics among the most unscrupulous originators.

HUD should go further in standardizing and simplifying the GFE and settlement statement. HUD must require the prominent disclosure of the annual percentage rate ("APR") on the GFE. In addition, as discussed below, without substantive regulation of yield spread premiums that permits them only in the case of no-cost loans, where homeowners can realize the potential benefits of lender-paid broker compensation, homeowners nevertheless will continue to make costly errors in purchasing home-secured credit.

A. The Early and Binding Provision of the GFE is Essential for Consumer Shopping

We applaud HUD for requiring that the GFE be provided early and at a uniform time in the mortgage shopping process.

HUD proposes to only require that the GFE be held binding for 10 business days before a complete mortgage application is submitted.[7] This does not seem to be sufficient time for consumers to shop for a different mortgage, obtain alternative GFEs, compare them and then make the decision to return to a particular originator, particularly without requiring an interest rate lock. More importantly, it does not seem to be sufficient time even to close on the loan for which the GFE is offered.

Industry practice generally assumes that in the purchase-money context a minimum of 30 days is needed to shop for and obtain a binding mortgage commitment.[8] If an interest rate lock is required, such a short time frame might be legitimate to protect lenders from interest rate fluctuations. Without a mandated interest rate lock, however, the short time frame is useless. While interest rates might fluctuate over 30 days significantly, settlement costs are unlikely to fluctuate at all. Certainly, lenders should be able to predict the settlement costs with a high degree of certainty a month in advance. *Accordingly, the GFE should be binding for at least 30 days.*

Moreover, a GFE must include an interest rate lock. Without an interest rate lock, consumers can only shop on the settlement costs of the loan, not the interest rate. The

[7] 73 Fed. Reg. 14030, 14057 (Mar. 14, 2008).

[8] *See, e.g.,* Woodbury Title Goup, The Closing Process, http://www.woodburytitle.com/page/page/2189688.htm (most mortgage contingency clauses in contracts specify 30-45 days to shop for a mortgage).

failure to require an interest rate lock undermines the effectiveness of the early provision of the GFE. Interest is the largest component of the price of a mortgage. If interest rates are allowed to float while settlement costs are fixed, consumers are encouraged to shop on the smallest portion of mortgage costs, the settlement costs, and lenders are encouraged to play bait and switch games with the offered interest. *To be a useful shopping tool, all costs must be fixed at the time the GFE is delivered.*

In order to encourage shopping, HUD permits the charging of only two fees, for the cost of providing the GFE and a credit report.[9] While the intent is good, this provision potentially runs afoul of both federal and state consumer protection provisions. RESPA itself forbids the charging of any fees for the preparation of the final settlement statement.[10] HUD's endorsement of a fee on the GFE, the necessary precursor to the settlement statement, undercuts this prohibition.[11] *Accordingly, we recommend that HUD not mention any fees in relation to the GFE. The cost of providing a GFE is simply a cost of doing business, and there is no reason for HUD to encourage – and sanction – the addition of a new fee.*

Despite the promise of this rulemaking, it remains likely that the requirement that the GFE be delivered early in the mortgage application process will be honored more in the breach than in actuality. Without aggressive enforcement by HUD and a private right of action for consumers, as discussed below, lenders will not have sufficient incentives to make sure that consumers are supplied with shopping tools in a timely fashion. HUD assumes repeatedly that its new rules will change the marketplace and cause unscrupulous originators to become more transparent.[12] However, there are no teeth in the regulation. Currently, many borrowers never receive a GFE, and many of those who do so receive it at closing. Without enforcement by consumers on both the time of delivery and the accuracy of the numbers, GFEs are likely to continue to be used as much as a tool for bait and switch as for honest competition.

B. A Standardized GFE that Focuses Consumer Attention on the Key Price

[9] 73 Fed. Reg. 14030, 14057 (Mar. 14, 2008).

[10] 12 USC §2610.

[11] Implicitly, authorizing the charging of a fee for the preparation of a GFE encourages lenders to pass on to consumers at the GFE stage the costs of preparing the final settlement statement. Moreover, some states prohibit the charging of any nonrefundable application fee before the credit is issued. HUD's proposal could be seen to preempt those state statutes by permitting the charging of a fee. Similarly, the model GFE has a space for the lender to fill out the amount of an application fee.

[12] Office of Pol'y & Dev., Dep't. of Hous. & Urban Dev., RESPA: Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis, FR-5180-P-01: Proposed Rule to Improve the Process of Obtaining Mortgages and Reduce Consumer Costs, 3-58 (2008) ("[T]his table makes it more likely that . . . originators will [explain loan options] since the failure to do so might result in a bunch of questions on the topic, and a change in the loan requested, and the need to write-up a new GFE.").

Components is Critical

The new GFE is standardized and legible. It does a very good job of letting a consumer do what the GFE was designed to do: choose the cheaper loan when the difference is all in the settlement costs.

Consumers need a standardized and streamlined GFE in order to be able to shop. The current GFE provides too much information and does not point to the most important costs. Most consumers can tolerate no more than three or four decision points.[13] Compare this to the 45 separate fees listed on a single GFE reviewed by HUD in its Economic Analysis.[14] Few, if any, borrowers are able and willing to aggregate so many disparate fees. Only 13% of consumers have the quantitative literacy to add fees in order to compare prices,[15] even if they were willing and could take the time to do so. Aside from the math, borrowers have trouble just identifying fees when presented with a long list.[16] The current

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[13] For example, most consumers in credit card shopping will only look at two pieces of information. Jinkook Lee & Jeanne M. Hogarth, *Relationships among Information Search Activities When Shopping for a Credit Card*, 34 J. Consumer Aff. 330, 340 (2000). Similarly, in reviewing credit card activity, most borrowers only look at three categories of information in evaluating the card and their continued use of the card. Macro International, Inc., Design and Testing of Effective Truth in Lending Disclosures 19 (2007), http://www.federalreserve.gov/dcca/regulationz/20070523/Execsummary.pdf. The three categories reported were information about payments, the account activity summary, and the transaction list. Most other information was disregarded. Some evidence suggested that even the account activity summary was largely disregarded in favor of the transaction list. *Id.* at 31.

[14] Office of Pol'y & Dev., Dep't. of Hous. & Urban Dev., RESPA: Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis, FR-5180-P-01: Proposed Rule to Improve the Process of Obtaining Mortgages and Reduce Consumer Costs, 3-154 (2008).

[15] *See Mark Kutner, Elizabeth Greenberg & Justin Baer,* U.S. Department of Education, Institute of Education Sciences, National Center for Education Statistics, A First Look at the Literacy of America's Adults in the 21st Century 3, 4 (2005), *available at* http://nces.ed.gov/NAAL/PDF/2006470.PDF (only 13% of the adult population has quantitative proficiency; a "sample task "typical of level" is "computing and comparing the cost per ounce of food items").

[16] For example, when reviewing model disclosure forms with focus groups, half of the respondents in a survey conducted for the Federal Reserve missed at least one fee charged on a sample credit card statement. Macro International, Inc., Design and Testing of Effective Truth in Lending Disclosures 12, 40-41 (2007), http://www.federalreserve.gov/dcca/regulationz/20070523/Execsummary.pdf. Only when the researchers grouped and totaled the fees did the borrowers consistently find the fees. Similarly, in a recent survey conducted for the Federal Trade Commission ("FTC"), consumers reviewing mortgage disclosures were unable to identify or aggregate fees, although the listed fees were fewer than 20.As Herbert Simon points out, the easier it is to discover a satisfactory solution, the higher the standard for an acceptable solution becomes. Herbert A. Simon, *A Behavioral Model of Rational Choice,* 69 Q. J. Econ. 99, 111 (1955). *See also* Yu-Chun.Regina Chang & Sherman Hanna, *Consumer Credit Search Behavior*, 16 J. Consumer Studies and Home Economics 207

marketplace, where fees are listed by hundreds of different names, on a multitude of different lines, does not permit comparison shopping.[17]

Totaling and aggregation of fees is therefore critical. The easier it is to shop the more likely it is that consumers *will* shop, and shop effectively. We must take care, however, to make sure that we focus consumers on the important and relevant totals, not irrelevant subtotals.

The standardization of the GFE will promote consumer shopping and facilitate market transparency. To ensure that the GFE is useful and not misleading to consumers, HUD must make the following further revisions:

- Replace the interest rate disclosure on the GFE with the APR.
- Provide only the earliest date on which the interest rate can rise, not the maximum (while retaining disclosure of the maximum payment—a key price measure for consumers).
- Reduce the focus on settlement costs, by reducing the font size and eliminating the bold for settlement costs.
- Only provide a total for all settlement costs on the first page of the GFE, without breaking out the origination costs.
- Provide guidance to originators as to the calculation of the maximum payment and maximum loan balance.

C. The Proposed GFE Must Include the APR as the Key Loan Term

(1992) (consumers seek a solution that meets minimum requirements without expending too much energy).

[17] The National Consumer Law Center has collected and analyzed over 981 settlement statements. The settlement statements tend to be more uniform than the GFEs, but even among the settlement statements there is wide disparity. On the 981 settlement statements analyzed, there were 326 different fee names used in the 800 series, 221 different fee names in the 1110 series, and 133 different fee names in the 1300 series. The same fees were reported with different names and on different lines more often than not. Nat'l Consumer Law Ctr., *Lenders' Use of the HUD-1 and HUD-1A Settlement Statements: An Early Analysis of Data from the National Mortgage Data Repository 3-4* (Aug. 2007). HUD's analysis of 3000 settlement statements from five metropolitan areas, shows comparable divergence, with over 130 different fee names in the 800 series and nearly 200 different names in the 1100 series. Office of Pol'y & Dev., Dep't. of Hous. & Urban Dev., *RESPA: Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis, FR-5180-P-01: Proposed Rule to Improve the Process of Obtaining Mortgages and Reduce Consumer Costs, 3-155 – 3-159* (2008).

HUD is focused on reducing costs for consumers and facilitating shopping. The APR, in the mortgage market, is a necessity to achieve those goals.

The APR is the only apples-to-apples shopping metric in the mortgage market.[18] Its consistent use reduces the cost of consumer credit.[19] Consumers look for and rely on the APR when shopping. In 2000, ninety-one percent of the population was "aware" of the APR.[20] More than seventy percent of the population reports using the APR to shop for closed-end credit.[21] Seventy-eight percent of homeowners who refinanced their homes report comparison shopping on the basis of the APR.[22]

If the goal is to facilitate consumer shopping for mortgages, *HUD must mandate the inclusion of the APR on the GFE.* Interest rates are not as useful and can undermine the disclosure of the APR.

Interest rates, while reflecting the largest cost of credit, do not bundle all costs. Reliance on an interest rate in shopping can result in taking out the more expensive loan overall. Depending on the term of the loan, the fees, and how the rate is stated and calculated, interest rates can be inherently misleading and deceptive and quite often are not comparable with each other.[23] Moreover, interest rates do not control for the term of the loan.

Unlike interest rates, the APR takes the total cost of the loan, including fees and the time cost of money, and scales that cost to the size and term of the loan. The APR bundles the fees with the interest rate and standardizes the rate over an annual term. Thus, a shopper can tell whether a 15 year loan is cheaper than a 30 year loan by looking at just one number, no matter how many fees the lender has piled on at origination.

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[18] *See, e.g.*, Elizabeth Renuart & Diane E. Thompson, *The Truth, the Whole Truth, and Nothing But the Truth: Fulfilling the Promise of Truth in Lending*, 25 Yale J. on Reg. 181 (2008).

[19] *See* Victor Stango & Jonathan Zinman, *How a Cognitive Bias Shapes Competition: Evidence from Consumer Credit Markets* 3-4, Sept. 5, 2006, http://papers.ssrn.com/sol3/papers.cfm?abstract_id=928956 (in markets where TILA disclosures made reliably, consumers who most underestimate APRs given a payment stream do not overpay on credit; in markets where TILA disclosures not made reliably, same consumers pay 200-400 basis points more for interest compared to consumers who underestimate APRs to a lesser degree).

[20] Thomas A. Durkin, *Credit Cards: Use and Consumer Attitudes, 1970-2000*, Fed. Res. Bull., 623, 631 (Sept. 2000), http://www.federalreserve.gov/pubs/bulletin/2000/0900lead.pdf.

[21] Jinkook Lee & Jeanne M. Hogarth, *The Price of Money: Consumers' Understanding of APRs and Contract Interest Rates*, 18 J. Pub. Pol'y & Marketing 66, 74 (1999).

[22] Jinkook Lee & Jean M. Hogarth, *Consumer Information Search for Home Mortgages: Who, What, How Much, and What Else?*, 9 Fin. Services Rev. 277, 286 (2000).

[23] *See generally* Christopher L. Peterson, *Usury Law, Payday Loans, and Statutory Slight of Hand: Salience Distortion of American Credit Pricing Limits*, 92 Minn. L. Rev. 1110 (2008).

In recent years, the marketing of payment option ARMs has underscored the need for uniform disclosure of and reliance on the APR and the problems with the use of interest rates in disclosure. Payment option ARMs are typically advertised as, for example, "a 2% fixed rate" even though this rate may be fixed for no more than a day.[24] The APR, while it does not entirely reflect the risk of upwards adjustments in the interest rate, given problems with how it is calculated,[25] at least reduces the distortion, by requiring that the rate disclosed be a composite rate.[26] Composite rates reflect both an initial low rate and the rate that would be in effect but for the initial teaser rate.

Consumers cannot do the math to determine which of two loans is cheaper, given different rates, different fees, and different terms. The APR solves that problem and permits consumers to shop intelligently and efficiently. Failing to include the APR on the GFE obscures the cost of credit and hinders consumer shopping.

It is no answer to suggest that consumers can rely on an early TIL disclosure for the APR. Even when the early TIL disclosure is provided, there is no penalty for providing an inaccurate TIL disclosure, whether accidentally or intentionally. As a result, many of the early TIL disclosures actually provided in the current marketplace are misleading.

Moreover, if the GFE is to have its maximum effect, it should be the single shopping tool for the mortgage. If consumers have to use multiple sheets to shop, the usefulness of the GFE is considerably diluted. Permitting multiple summary sources of critical information virtually guarantees that some consumers will ignore one or the other source. Ignoring the settlement costs and key loan terms reflected on the GFE would be undesirable. Ignoring the APR would be disastrous in most cases. Thus, if the GFE is to be used for shopping, disclosure of the actual APR must be mandated by HUD.

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[24] *See, e.g.,* Andrews v. Chevy Chase, 240 F.R.D. 612 (E.D. Wis. 2007) (describing payment option ARM sold as having a fixed rate, when interest varied monthly; fixed rate is the payment rate); Complaint at 4, Fed'l Trade Comm'n v. Chase Financial Funding, Inc., No. SACV04-549 (C.D. Ca. 2004), *available at* http://www.ftc.gov/os/caselist/0223287/040602comp0223287.pdf (adjustable rate mortgage with initial minimum payment, based on interest at 3.5% amortized over 30 years, which results in negative amortization, since actual interest rate is much higher, advertised as "3.5% fixed payment 30 year loan."); Gov't Accountability Office, GAO No. 06-1021, Alternative Mortgage Products: Impact on Defaults Remains Unclear, but Disclosure of Risks to Borrowers Could Be Improved 22 (2006), *available at* http://www.gao.gov/new.items/d061021.pdf (describing advertisement for payment option ARM that promised 45% reduction in monthly mortgage payments and interest rate of 1.25%; interest rate of 1.25% only applied for first month, and this fact disclosed in "much smaller print" on second page).

[25] Patricia A. McCoy, *Rethinking Disclosure in a World of Risk-Based Pricing*, 44 Harv. J. on Legis. 123, 143-44 (2007) (discussing limitations of variable rate disclosures in detail).

[26] 12 C.F.R. §226.17, Official Staff Commentary, §226.17(c)(1)-(10).

D. Explanation of NCLC's Recommended GFE Form

Following is our recommended summary GFE form. The key elements of a standard summary GFE should include:

- The APR
- The maximum payment, in dollars
- The maximum loan balance, in dollars
- The total closing costs, in dollars
- Information regarding whether the rate can rise, and the earliest date on which the rate can rise

A second page could have a tradeoff box and detailed information about mortgage broker compensation. (This should not be on the first page of the GFE).

The summary GFE should NOT have:

□ The interest rate
□ Subtotals of costs or fees

Appendix 1 provides an example of NCLC's model summary GFE form. As discussed above, absent statutory and regulatory changes creating a fee-inclusive TIL finance charge, the final settlement statement provided must contain a detailed itemization of all charges. Any detail provided on the GFE should match that provided on the final settlement statement, but should follow on separate pages, in order not to detract from the summary.

5. <u>The Potential Challenges with Implementing the Proposed "Closing Script"</u>

As demonstrated by HUD's consumer testing, consumers like and benefit from an oral explanation of their loan terms at closing.[27] Such information is seldom forthcoming at current closings. If the requirement were taken seriously by closing agents, it could impede the rushed closings that many consumers, particularly in the subprime market, experience and facilitate a better opportunity for consumers to understand some of the important features of their loans.[28]

However, the closing script has two critical omissions: the APR and notice of the consumer's three-day right of rescission for non-purchase money mortgage transactions.

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[27] U.S. Dep't of Housing and Urban Dev., Office of Pol'y Dev.& Research, RESPA Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis: Proposed Rule to Improve the Process of Obtaining Mortgages and Reduce Consumer Costs 3-46 (2008).

[28] *Sprague v. Household Intern.*, 473 F. Supp. 2d 966, 972 (W.D. Mo. 2005) (describing closings of real estate loans in less than ten minutes at fast food restaurants and delis).

The failure to mention and correctly explain the right of rescission in the closing script will undermine the clear and conspicuous disclosure of the right of rescission as required by TILA. Again, this is another area where coordination with the Federal Reserve Board regulation of TILA is essential.

Moreover, given the wide history of fraud by closing agents,[29] HUD should take care when providing a seal of approval to the oral statements of any closing agents. HUD may be able to prescribe the words, but it is unlikely to be able to monitor the tone in which they are delivered, or whether those exact words actually were used. Two alternative scenarios are possible. In one case, a closing agent may rush through the script and downplay its importance: "This is just something the government makes me say." In another case, a closing agent could say, "You can trust me. What I am telling you has been approved by HUD. This is a government approved loan." Neither scenario results in the transparency envisioned by HUD. Both could exacerbate existing problems of misplaced trust in the settlement process.

It is not clear how delivery of the closing script would be enforced. Consumers might have a private right of action for deception under state law, but settlement agents routinely have consumers sign an acknowledgment that the settlement agent is not the borrower's agent and that the borrower agrees to indemnify the settlement agent for any misstatements. HUD should clarify that both the lender and the closing agent are responsible for ensuring the good faith delivery of the closing script and that borrowers have a right to rely on the accuracy of the closing script. Absent enforceability and clear direction from HUD, the closing script may be abused or not delivered as often as it is given in a helpful manner to borrowers. Current RESPA compliance failures make this possibility likely.

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[29] *See, e.g.*, Nationwide v. Echeverria, 725 N.W.2d 659 (Iowa App. 2006) (title company disbursed loan proceeds to seller although seller did not have title to property and outstanding mortgage lien on property); Matter of Harris, 2006 NY Slip Op 9317 (N.Y. App. Div. 2006) (attorney disbarred after being sentenced to 18 years in prison and restitution of $100,000 in property flipping scheme); United States v. Lutz, 2006 WL 3716581 (4th Cir. Dec. 14, 2006) (upholding "willful blindness" instruction to jury when evidence showed that closer concealed the property flip from lenders by disguising loan disbursements and concealing rapid transfers of property); United States v. Wilkins, 2007 WL 896147 (E.D.Tenn. March 22, 2007) (title company explained two HUD-1s to buyer, including fact that buyer was making a false statement);American Title Co. of Houston v. Bomac Mortg. Holdings, L.P., 196 S.W.3d 903 (Tex.App. 2006), *review granted, judgment vacated, and remanded by agreement* (Mar. 16, 2007) (discussing title company alteration of HUD-1 and title report to conceal source of down payment and flip of property); David Cho, *Housing Boom Tied to Sham Mortgages, Lax Lending Aided Real Estate Fraud,* Wash. Post., Apr. 10, 2007, at A1 (closing attorneys convicted as accomplices in large property flipping scheme) United States. v. Sloan, 505 F.3d 685 (7th Cir. 2007) (reviewing restitution order entered against paralegal who participated in property flipping scheme with attorney-employer).

In addition, the closing script could be used by both closing agents and lenders to absolve themselves of responsibility for misrepresentation. In this respect the acknowledgment is particularly troubling. Unscrupulous or simply harried closing agents may be tempted to add the acknowledgment page to the stack of documents a borrower signs at closing with no more than a hurried, "sign here." Regardless of whether there were inconsistencies or whether or not they were explained, lenders and closing agents are likely to use the acknowledgment as a safe harbor, absolving them from all responsibility for abusive practices. The acknowledgment of the closing script could be used against borrowers.

For the closing script to function as envisioned by HUD, at a minimum make the following changes must be made:

- *Delete the acknowledgment.*
- *Require the APR to be disclosed.*
- *Require the notice of the right to cancel be disclosed, where applicable.*
- *Clarify that lenders are responsible for the accurate delivery of the closing script.*
- *Clarify that settlement agents also are responsible to the borrower for the accurate delivery of the closing script.*

6. The Benefits and Limitations of the Disclosure of Yield-Spread Premiums to Consumers

Lender-paid broker compensation, as HUD describes, leads to higher settlement costs and higher broker costs, as well as higher interest rate costs.[30] In most circumstances, borrowers receive little, if any, benefit from lender-paid broker compensation. Even worse, lender-paid broker compensation appears to drive racially disparate pricing. Only where the fees are either all in or all out of the rate are consumers able to shop successfully for the cheapest loan. When consumers can compare loans with the fees all *in* or all *out,* they are comparing loans with a limited number of variables. On the one hand is a loan with a particular rate and all fees required to be paid by the borrower – which would have to come from either cash or the home equity (meaning that the fees would be paid for in the loan, and more would be borrowed). On the other hand is the same loan with all of the fees paid through the interest rate – so no additional cash would required from the borrower and the loan amount would not have to be increased to cover the closing costs – yet the interest rate would be slightly higher. The latter loan is often called in the industry a "no-cost loan." This is somewhat of a misnomer because there are fees charged on these loans, and paid for by the consumer, only through a higher rate.

There are multiple benefits for "no-cost loans." These include the obvious – the retention of precious cash and equity by the borrower – as well as the lesser known finding

[30] Office of Pol'y & Dev., Dep't. of Hous. & Urban Dev., RESPA: Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis, FR-5180-P-01: Proposed Rule to Improve the Process of Obtaining Mortgages and Reduce Consumer Costs, 2-24 - 2-43 (2008).

that "no-cost" loans can result in a significant reduction of all closing costs as compared to other loans.[31] *However, the key to achieving this reduction is that the lender pays ALL of the fees.* The use of a combination of methods of payments – cash or home equity from the borrower plus lender paid broker compensation – has just the opposite effect: an increase in the closing costs and loan costs. Disclosure, by itself, does not overcome the cognitive dissonance caused by splitting the fees.

Disclosing lender-paid broker compensation is difficult. Most disclosures of lender-paid broker compensation are likely to confuse consumers, both because the tradeoffs are inherently complex and because borrowers are led to believe erroneously by both brokers and originators that brokers act as the borrowers' agents.[32] We concur with HUD that the yield spread premium should not be disclosed on a separate agreement. We share HUD's concerns that a separate agreement is likely to cause confusion to borrowers. We agree that the impact of any permissible yield spread premium must be clearly disclosed on the GFE. However, HUD's use of the term "credit" to describe the lender-paid broker compensation, in the absence of substantive regulation that limits total fees, is misleading. Empirically, when there is a mix of both borrower-paid and lender-paid broker compensation, the total of all fees *increases*. When there is this combination of methods of payments, there is not a one-for-one reduction in the borrower's costs, as the common understanding of the word "credit" would convey.

Lender paid broker compensation, when combined with borrower paid closing costs, is particularly troubling because it contributes to the widespread disparities in the pricing of home mortgage loans between whites and African Americans and Latinos. These disparities exist at every income and credit level and increase as income and credit levels increase.[33] In

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[31] Borrowers who use "no-cost" loans and so can shop on interest rate alone pay $1,200 less than borrowers who pay some lender or broker fees in cash. This suggests that consumers have a tougher time comparing alternatives when trade-offs are involved and that mortgage loan markets are not fully transparent or competitive. Susan Woodward, *A Study of Closing Costs on FHA Mortgages*, U.S. Department of Housing and Urban Development, Office of Policy Development and Research. (2008.), available at http://www.urban.org/UploadedPDF/411682_fha_mortgages.pdf.

[32] The Federal Reserve Board recently withdraw its proposed regulation of mortgage broker disclosure after consumer testing revealed that even when the disclosure included an explicit disavowal of the broker's agency, most consumers, even in a testing situation, without active misrepresentation by a broker, continued to believe that the broker, paid for by the consumer, was acting in the consumer's best interests. 73 Fed. Reg. 44,522, 44,564 (July 30, 2008).

[33] *See, e.g.,* Robert B. Avery, Kenneth P. Brevoort & Glenn B. Canner, *The 2006 HMDA Data,* Fed. Reserve Bull. A73, A97 (2007), *available at* http://www.federalreserve.gov/pubs/bulletin/2007/pdf/hmda06final.pdf (in 2006 and 2005, African Americans and Hispanics who received higher cost loans, on average, after accounting for borrower characteristics and lender, paid 20 and 10 basis points more, respectively, than white borrowers also in the subprime market); *see also* Marsha J. Courchane, *The Pricing of Home*

other words, the wealthiest and most credit worthy African Americans and Latinos are, compared to their white counterparts, the most likely to end up with a subprime loan. The origination channel – whether or not a loan is brokered – accounts for most of the difference in pricing.[34]

Mortgage Loans to Minority Borrowers: How Much of the APR Differential Can We Explain?, 29 J. Real Est. Res. 399, 417 (2007) (in 2005, African Americans and Hispanics who received subprime loans paid, on average, 50 and 17 basis points more, respectively, than whites in the subprime market); Debbie Gruenstein Bocian, Keith S. Ernst & Wei Li, Ctr. For Responsible Lending, Unfair Lending: The Effect of Race and Ethnicity on the Price of Subprime Mortgages 11 (May 31, 2006), *available at* http://www.responsiblelending.org/pdfs/rr011-Unfair_Lending-0506.pdf *see also* Jim Campen, *Borrowing Trouble VII: Higher-Cost Mortgage Lending in Boston, Greater Boston and Massachusetts, 2005* at 8 (Mass. Community & Banking Council, Jan. 2007), *available at* www.masscommunityandbanking.org (highest income Latinos received high-cost home purchase loans at 6 times the rate of the highest income whites; highest income African Americans 7.6 times to receive a high-cost home purchase loan than highest income whites); Geoff Smith, Woodstock Institute, Key Trends in Chicago Area Mortgage Lending: Analysis of Data from the 2004 Chicago Area Community Lending Fact Book 10 (2006) (African-Americans and Hispanics more likely to receive high-cost loan than white borrowers, disparity increases as income increases); Elvin K. Wyly, Mona Atia, Holly Foxcroft, Daniel J. Hamme, Kelly Phillips-Watts, *American Home: Predatory Mortgage Capital and Neighbourhood Spaces of Race and Class Exploitation in the United States*, 88 Geografiska Annaler, Series B: Human Geography 105 (2006) (finding geographic racial disparities in lending in Baltimore that cannot be explained by income); Stephanie Casey Pierce, Racial Disparities in Subprime Home Mortgage Lending: Can the Difference Be Explained by Economic Factors? (2006) (unpublished M. Pub. Pol'y thesis, Georgetown University), *available at* http://www.dspace.wrlc.org/bitstream/1961/3612/1/etd_smc54.pdf (a survey of 2004 HMDA data from Louisiana found that blacks were 13.82% more likely than whites to receive a high cost, first lien purchase loan); *cf.* Robert B. Avery, Kenneth P. Brevoort, & Glenn B. Canner, *Higher Priced Home Lending and the 2005 HMDA Data*, Fed. Reserve Bull. A123, A138 (2006) (piggyback loans more common in minority census tracts, even holding income constant), *available at* http://www.federalreserve.gov/pubs/bulletin/2006/hmda/bull06hmda.pdf.

[34] *See* Robert B. Avery, Kenneth P. Brevoort & Glenn B. Canner, *The 2006 HMDA Data,* Fed. Reserve Bull. A73, A96 (2007), *available at* http://www.federalreserve.gov/pubs/bulletin/2007/pdf/hmda06final.pdf (pricing disparities between whites and minorities highest for broker originated loans); Robert B. Avery, Kenneth P. Brevoort, & Glenn B. Canner, *Higher Priced Home Lending and the 2005 HMDA Data*, Fed. Reserve Bull. A123, A157-58 (2006), *available at* *http://www.federalreserve.gov/pubs/bulletin/2006/hmda/bull06hmda.pdf* (same); Robert B. Avery & Glenn B. Canner, *New Information Reported under HMDA and Its Application in Fair Lending Enforcement*, Fed. Reserve Bulletin 344, 380, 394 (Summer 2005), *available at* http://www.federalreserve.gov/pubs/bulletin/2005/3-05/hmda.pdf (same); *cf.* Marsha J. Courchane, *The Pricing of Home Mortgage Loans to Minority Borrowers: How Much of the APR Differential Can We Explain?*, 29 J. Real Est. Res. 399, 400 (2007) ([M]uch of the explanation for why minority borrowers tend to have higher APRs than non-minority borrowers

Lender-paid broker compensation creates the incentives that drive much of the racially disparate pricing.[35] By encouraging brokers to overprice loans where and when they can, lenders implicitly encourage brokers to target the vulnerable and gullible and those perceived as vulnerable and gullible. Most borrowers naively believe that their lenders will give them the loan they qualify for, and are insufficiently on their guard in dealing with brokers. African Americans and Latinos are particularly likely to believe that lenders are required to give them the best rate for which they qualify.[36]

The mechanics and extent of lender-paid broker compensation reach beyond simply overcharging African-American and Latino borrowers. Lenders use broker compensation to lock African-Americans and Latinos into downwardly mobile borrowing and destructive products. For example, lender payments to brokers are often conditioned on the borrower's acceptance of a prepayment penalty.[37] Thus, brokers have an incentive not only to put borrowers into a high cost loan in order to receive additional compensation from the lender, but to make sure the borrower is locked into the high cost loan. Prepayment penalties in these circumstances are seldom chosen by the borrower or in the borrowers' interest.[38]

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is because minority borrowers disproportionately take out subprime loans."); William Apgar, Amal Bendimerad & Ren S. Essene, Joint Ctr. for Housing Studies, Harvard Univ., Mortgage Market Channels and Fair Lending: An Analysis of the HMDA Data 27, 37 (2007), *available at* http://www.jchs.harvard.edu/publications/finance/mm07-2_mortgage_market_channels.pdf (white borrowers 50% more likely than African American borrowers to get a loan from a CRA-regulated entity within its CRA assessment area; failure to get a loan from a regulated institution within its catchment area increases the cost of the loan).

[35] Debbie Gruenstein Bocian, Keith S. Ernst & Wei Li, Ctr. For Responsible Lending, Unfair Lending: The Effect of Race and Ethnicity on the Price of Subprime Mortgages 21-23 (May 31, 2006), *available at* http://www.responsiblelending.org/pdfs/rr011-Unfair_Lending-0506.pdf (discussing evidence and analysis that links pricing disparities with broker activity and incentives); *see also* Press Release, Office of the New York State Attorney General, Countrywide Agrees to New Measures to Combat Racial and Ethnic Disparities in Mortgage Loan Pricing (Dec. 5, 2006), *available at* http://www.oag.state.ny.us/press/2006/dec/dec05a_06.html (pricing disparities between whites and minorities highest for broker originated loans).

[36] Mortgage Foreclosure Filings in Pennsylvania: A Study by The Reinvestment Fund for the Pennsylvania Department of Banking 74 (Mar. 2005), *available at* http://www.trfund.com/policy/pa_foreclosures.htm , *citing* Fannie Mae's 2002 National Housing Survey.

[37] *See* Debbie Gruenstein Bocian, Keith S. Ernst & Wei Li, Ctr. For Responsible Lending, Unfair Lending: The Effect of Race and Ethnicity on the Price of Subprime Mortgages 21 (May 31, 2006), *available at* http://www.responsiblelending.org/pdfs/rr011-Unfair_Lending-0506.pdf (noting that payment of yield spread premiums is often conditioned on the imposition of a prepayment penalty).

[38] Loans with prepayment penalties attached have higher rates of foreclosure, and in brokered loans, borrowers generally receive no interest rate reduction in exchange for the imposition of the prepayment penalty. *See, e.g.,* Morgan J. Rose, Predatory Lending Practices

The key point here is – *Disclosure by itself is unlikely to remedy the systematic abuses of lender paid broker compensation HUD identifies.*

A. Lender Payments to Brokers Should Not Be Characterized As a Credit

HUD's proposal to describe lender-paid broker compensation as a *credit* used to reduce settlement costs is inherently misleading. There is no requirement that the lender payment will actually be used in that manner. Nothing in the proposed rule requires that brokers only be compensated through a yield spread premium or that the lender payment to the broker be offset against the total broker price charged to the borrower. Merely having the lender payment shown as a borrower credit to reduce the settlement costs will not make it function that way: Brokers can still charge borrowers a separate or increased fee.

It is simply not true, as HUD proposes to emblazon on the GFE, that a lender-paid broker payment reduces upfront costs. In most cases, according to studies HUD cites, lender-paid broker payments actually increase upfront costs.[39]

The treatment of the lender payment to the broker as a credit also potentially

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and Subprime Foreclosures – Distinguishing Impacts by Loan Category 45 (Dec. 2006), *available at* http://www.chicagofed.org/cedric/2007_res_con_papers/car_62_morgan_j_rose_foreclosures_draft.pdf (prepayment penalties and balloon notes combined on a fixed rate refinance subprime loan increase the rate of foreclosure 227%); Ellen Schloemer, Wei Li, Keith Ernst & Kathleen Keest, Ctr. For Responsible Lending, Losing Ground: Foreclosures in the Subprime Market and Their Cost to Homeowners 21 (Dec. 2006), *available at* http://www.responsiblelending.org/pdfs/foreclosure-paper-report-2-17.pdf (higher risk for foreclosure for adjustable rate loans, loans with balloon payments, loans with prepayment penalties, and limited documentation); Gregory Elliehausen, Michael E. Staten & Jevgenijs Steinbuks, *The Effect of Prepayment Penalties on the Pricing of Subprime Mortgages* 15 (Sept. 2006), *available at* http://www.chicagofed.org/cedric/2007_res_con_papers/car_79_elliehausen_staten_steinbuks_preliminary.pdf (finding that prepayment penalties were associated with higher interest rates unless they controlled for "borrower income, property value, loan amount, whether the loan was originated by a broker, and type of interest rate," in which case the difference shrank); *see also* Debbie Gruenstein Bocian, Keith S. Ernst & Wei Li, Ctr. For Responsible Lending, Unfair Lending: The Effect of Race and Ethnicity on the Price of Subprime Mortgages 3-4 (May 31, 2006), *available at* http://www.responsiblelending.org/pdfs/rr011-Unfair_Lending-0506.pdf (the presence of a prepayment penalty increased the likelihood that African Americans had a higher cost subprime loan as compared to whites).

[39] U.S. Dep't of Housing and Urban Dev., Office of Pol'y Dev.& Research, RESPA Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis: Proposed Rule to Improve the Process of Obtaining Mortgages and Reduce Consumer Costs 2-25 - 2-48 (2008).

complicates TIL review. Without guidance from the Federal Reserve Board, it is not entirely clear what effect treating the lender paid broker compensation as a borrower credit will have on the central TIL disclosures, the finance charge and the APR. The credit should be treated as an additional down-payment that reduces the principal loan amount but is otherwise neutral as to the calculation of these central disclosures. Yet without guidance from the Federal Reserve Board, the use of the word "credit" opens up a litigation minefield and likely increases costs for all parties.

A more honest and transparent disclosure about the effect of the yield spread premium is illustrated in Appendix 2 of this Testimony.

The problem is not that brokers are paid out of the interest rate: the problem is that brokers are paid *both* out of the interest rate and out of pocket (or equity). HUD recognizes the costs borrowers incur when borrowers must shop both on fees and rate.[40] Yet the proposal would substitute *disclosure* for substantive regulation. If HUD were to require – as part of its regulation under RESPA's section 8 (12 U.S.C. Section 2607) – that lender paid fees be actually credited to borrower's previously enumerated costs, then this mechanism might work as HUD envisions. But simply requiring a disclosure would not make the lender paid fee provide a reduction dollar for dollar to the borrower.

B. Lender-Paid Broker Compensation Should Only Be Permitted for No-Cost Loans

Given the extensive evidence HUD cites that fees and borrower confusion are at their highest when brokers are paid both by the borrower and the lender,[41] lender-paid broker compensation should only be permitted for no-cost loans.[42]

True no-cost loans, where all fees are pushed into the rate, can offer significant benefits for consumers and the market. Consumers appear to maximize their shopping return with no-cost loans. Racial disparity in pricing appears to vanish in no-cost loans.[43]

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[40] *Id.*

[41] *E.g.*, U.S. Dep't of Housing and Urban Dev., Office of Pol'y Dev.& Research, RESPA Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis: Proposed Rule to Improve the Process of Obtaining Mortgages and Reduce Consumer Costs 2-26, 2-34 (2008).

[42] In this situation, lenders must list all charges incurred in the transaction on the settlement statement but show them as P.O.C., paid outside of closing. *See* HUD Instructions in Regulation Z, 24 C.F.R. 3500 Appendix A. If the lender provides a credit to the consumer to cover closing costs, the credit must appear on lines 204-209 of the settlement statement. *See* HUD Letter Regarding Disclosures on Good Faith Estimate and HUD-1 Settlement Statement, Q 12, attached to OCC Advisory Letter AL 2000-5.

[43] U.S. Dep't of Housing and Urban Dev., Office of Pol'y Dev.& Research, RESPA Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis: Proposed Rule to Improve the Process of Obtaining Mortgages and Reduce Consumer Costs 2-43 (2008).

No-cost loans provide the proper incentives for originators and the secondary market. In a no-cost loan, the only money to be made is if the loan performs over time. Thus, no-cost loans give originators and the secondary market an increased incentive to make sure that underwriting is done at the time of origination. No-cost loans also reduce the incentive to strip equity by increasing the loan amount with junk fees. Such equity stripping does the consumer permanent harm and cannot be refinanced away, unlike a higher interest rate.

HUD should, under RESPA, define the payment of a yield spread premium, which increases the interest rate, at the same time as the borrower is being charged other up-front fees that purport to reduce the rate, as a kickback. There is substantial evidence that in these circumstances the yield spread premium increases total broker compensation and increases the borrower's cost, without providing any additional benefit to the borrower.[44] In these circumstances, the yield spread premium cannot reasonably be seen as a payment for other than the increased rate.

Yield spread premiums should be prohibited unless all other fees (other than escrow fees imposed in accordance with RESPA, actual government fees, and title insurance and title examination fees, if paid to an unrelated party and if bona fide and reasonable) are folded into the interest rate and no discount points are charged. Additionally, no other lender-paid broker compensation should be permitted if the borrower is making any direct payments to the broker.

7. Other Needed Legislative and Regulatory Changes to RESPA.

RESPA, although enacted with the noblest of intentions, lacks built in incentives to ensure compliance. **There is much that Congress can do to improve the settlement process in this nation by passing statutory changes to RESPA that would beef up enforcement.**

A. Civil Liability under RESPA and a Uniform Statute of Limitations Would Greatly Enhance Compliance

Without a private right of action to enforce the timing and content of both the GFE and the HUD-1 under sections 4 and 5 of RESPA, a borrower's leverage to negotiate loan terms and ensure fairness in the marketplace is severely limited. Civil enforcement of each element under the new rule, especially the GFE and HUD-1 requirements, is essential in order to raise levels of compliance and thus ensure a better functioning market.

We support HUD's intention to seek statutory modifications including authority for imposition of civil penalties for sections 4, 5, 6, 8, 9, and 10 of RESPA, as well as authority for the Secretary and state regulators to obtain injunctive and equitable relief under RESPA. Better enforcement mechanisms should result in some better compliance with these

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[44] *E.g.*, U.S. Dep't of Housing and Urban Dev., Office of Pol'y Dev.& Research, RESPA Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis: Proposed Rule to Improve the Process of Obtaining Mortgages and Reduce Consumer Costs 3-4 (2008).

requirements and the ability of state regulators to supplement the work of HUD is important.

Increased government enforcement, however, still leaves borrowers who were victims of "bait and switch" or other abusive lending with no recourse under RESPA sections 4 and 5 to directly challenge some of the main loan disclosures used to deceive them about loan terms. This is especially a concern in light of the new proposed GFE cover page. Without proper consequences for significant changes between the GFE cover page and the final loan disclosures, the GFE could be used as a tool to promote bait and switch regarding loan terms, as well as settlement costs, rather than for shopping. It could affirmatively aid in borrower deception because any misrepresentations would not be able to be stopped or challenged by the borrower. While undoubtedly some lenders would be deterred or punished through regulatory enforcement, the reach of regulatory measures is inevitably limited. As HUD itself points out in the proposed rule, without enforcement authority and clear remedies, consumers are less protected and the statute is much less effective. The remedy most likely to result in compliance is a private action by the borrower. Civil enforcement is a compliance incentive.

B. Section 8(b) Should Prohibit Overcharges, Not Only Markups.

Section 8(b)'s prohibition should apply to overcharges as well as markups. HUD has rightly indicated in its 2001 Statement of Policy[45] that unreasonable fees, even where a markup of a third-party fee is not involved, are prohibited under Section 8. We applaud HUD's inclusion of this approach in the Policy Statement, but unfortunately compliance with this provision has been limited. Every year, there are significant numbers of reported cases under Truth in Lending discussing unreasonable closing costs. We recommend that Congress clarify this by statutory language. While TILA requires the overcharges to be correctly disclosed as part of the finance charge and APR, TILA does not limit the amount of the overcharge.[46] RESPA could and should.

C. Escrow Collection Should Be Limited to the Amount Owed and Should Continue Even Where the Borrower Is 30 Days Late

Currently, servicers administering escrow accounts are permitted to collect payments so that the total paid on one year includes two extra months of funds. This practice has a particularly negative effect on homeowners who live on tight budgets, and the practice is not grounded in any reasonable expectation that such a cushion is necessary. Problems in escrow payments too often result in borrowers falling behind in their mortgage payments because the additional cost of taxes and insurance may not have been properly included in the underwriting, or because the cost of escrow has increased over time. For these homeowners,

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[45] Real Estate Settlement Procedures Act Statement of Policy, 2001-1, 66 FR 53052 (Oct. 18, 2001).

[46] 12 C.F.R. 226.4(c)(7).

the requirement of paying more than what is required to cover the month's payments is onerous and unwarranted. *We recommend that Congress change the rule so that only amounts owed can be collected through escrow.*

Moreover, *we recommend that either HUD or Congress clarify that a servicer must make escrow payments even where a homeowner is 30 days late on a payment.* We believe that the statute clearly requires that escrow payments must always be made by the servicer. The regulatory exception to this rule is unwarranted and causes substantial hurdles for borrowers seeking to straighten out their payments. Specifically, one payment made 30 days late is enough to jeopardize the borrower's homeownership if taxes go unpaid, fees and costs are then added to the tax bill, potentially doubling the tax bill. At that point, a small default—a late payment—may become insurmountable. This is especially a concern where one unpaid late fee could result in a borrower being categorized as 30 days late, even where all the relevant monthly payments for that month were paid on time and in full and where the late fee itself was incurred for paying late but substantially before the 30 day mark. This occurs because a borrower who owes a late fee but only sends in the usual monthly payment generally will have the payment applied first to the late fee and then to principal and interest, thus leaving insufficient funds to cover the regular payment. As a result, the monthly payment is not paid in full and is considered late. Borrowers who are 30 days late generally are not on their way to default. Interrupting escrow makes returning to on-time status harder to achieve – an unnecessary result.

D. RESPA's Servicing Rules Must Be Updated

Recent litigation challenging abusive mortgage servicing[47] and the challenges faced by

[47] *Islam v. Option One Mortg. Corp.*, 432 F. Supp. 2d 181 (D. Mass. 2006)(servicer continued to report borrower delinquent even after receiving the full payoff amount for the loan); *Hukic v. Aurora Loan Servicing, et al*, 2006 WL 1457787 (N.D. Ill. May 22, 2006)(servicer=s clerical error in recording amount of payment left homeowner battling with subsequent servicers and fending off foreclosure for nearly five years); *Rawlings v. Dovenmuehle Mortgage, Inc., 64 F. Supp. 2d 1156* (M.D. Ala. 1999)(servicer failed for over 7 months to correct account error despite borrowers' twice sending copies of canceled checks evidencing payments); *Choi v. Chase Manhattan Mortg. Co.*, 63 F. Supp. 2d 874 (N.D. Ill. 1999)(home lost to tax foreclosure after servicer failed to make tax payment from borrowers escrow account and then failed to take corrective action to redeem the property); *Monahan v. GMAC Mortg. Co.,* 893 A.2d 298 (Vt. 2005)(affirming $43,380 jury award based on servicer's failure to renew flood insurance policy and subsequent uninsured property damage); *Norwest Mortgage, Inc. v. Superior Court,* 85 Cal. Rptr. 2d 18 (Cal. Ct. App. 1999)(kickbacks available in force-placed insurance encourage placement); *Vician v. Wells Fargo Home Mortg.*, 2006 WL 694740 (N.D. Ind. Mar. 16, 2006) (servicers have forced-placed insurance in cases where the borrowers already had it and provided evidence of it); *Dowling V. Select Portfolio Servicing, Inc.*, 2006 WL 571895 (S.D. Ohio Mar. 7, 2006) (servicers have forced-placed insurance in cases where the borrowers already had it and provided evidence of it); *accord, Barbera v. WMC Mortgage Corp.*, 2006 WL 167632 (N.D. Cal. Jan. 19, 2006).

borrowers in the current foreclosure crisis make it clear that RESPA's servicing provisions need to be enhanced and updated. While HUD's current proposed rule focuses primarily on loan origination issues, some of the legislative changes HUD seeks look toward the post-origination phase. Escrow and servicing issues are essential to maintenance of a functioning mortgage market and to foreclosure prevention. In the current crisis, it is the servicing issues that have become paramount, yet the right to get a fair deal from a servicer is not uniformly enforceable and too often is out of reach for homeowners.[48]

- *First, RESPA must include a duty to provide reasonable loss mitigation prior to any foreclosure that prioritizes "home-saving" loss mitigation options over those that result in loss of the home.* Any loss mitigation must be based on an affordability analysis that considers the borrowers debt to income ratio and residual income—to ensure enough actual dollars for non-housing expenses—as well inclusion of the borrower's full debt profile, including junior liens on the property.

- Additionally, loan modification or forbearance agreements often contain a waiver of claims provision that purports to release the servicer and holder from any past or future claims that the borrower may have. Broad release language potentially cuts off all claims the borrower may have related to the origination or servicing of the loan; it must be banned. *RESPA also should prohibit the equally abusive practice of forcing borrowers to arbitrate any disputes with the lender or servicer.*

- Further, the current rules for responding to Qualified Written Requests do not allow a borrower to receive timely, useful information, nor do they prevent against foreclosures occurring before a response arrives. While RESPA currently requires servicers to respond to borrowers' request for information and disputes within 60 days, in practice many such inquires go unanswered. *RESPA should require that servicers respond to borrowers inquiries and disputes within 14 calendar days.* With a shorter timeline, a corresponding statutory change could then be made to remove the requirement for servicers to acknowledge receipt of QWRs. This timeline also would make it less likely that foreclosures would occur while QWRs are outstanding. *RESPA also should be amended to provide transparency to the servicing process by allowing the homeowner to obtain key information about the loan and its servicing history.* Such information should include:

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[48] These recommendations are incorporated in detail in H.R. 5679, The Foreclosure Prevention and Sound Mortgage Servicing Act of 2008, introduced by Representative Waters. NCLC has directly endorsed this legislation; it is a clear roadmap of some needed changes to RESPA's servicing rules. *See also* Written Testimony of Tara Twomey, National Consumer Law Center, also on behalf of National Association of Consumer Advocates, Before the Unites States House of Representatives Subcommittee on Housing and Community Opportunity, H.R. 5679, The Foreclosure Prevention and Sound Mortgage Servicing Act of 2008 (Apr. 16, 2008), *available at* http://www.nclc.org/issues/predatory_mortgage/content/TwomeyHR5679Testimony.pdf

- whether the account is current, or if not, the date the account went into default;
- the current balance due on the loan, including the principal due, an itemization of all fees due, an explanation of the escrow balance, and whether there is any escrow deficiency or shortage;
- a full payment history showing in a clear and easily understandable manner all the activity on the home loan since the origination of the loan, including the escrow account, and the application of payments;
- the initial terms of the loan; a copy of the original note and security instrument;
- identification of the owner of the mortgage note and any investors;
- any documents that limit, explain or modify the loss mitigation activities offered by the servicer; and
- any other information requested by the homeowner reasonably related to loss mitigation activities.

Finally, homeowners often have difficulty determining which address of the servicer is the correct one for sending QWRs. *RESPA should provide that any QWR received by the mortgagee or servicer is considered valid,* even where sent to an address other than one designated by the mortgagee or servicer for receipt and handling of such requests.

Conclusion

HUD has done an excellent job in moving the ball toward greater protection for consumers in the settlement process. The tweaks and adjustments that we recommend are important to ensure that the goal becomes the reality.

Appendix 1

NCLC MODEL SUMMARY GFE

Name of originator: ____________________ Borrower: ____________________

Originator Address: ____________________ Property address: ____________________

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Originator Phone number: ____________________ Date of GFE: ____________________

These loan terms are available until ________. After that date, the loan terms and closing amounts can change.

Summary of loan terms	Cost of loan		
	APR*	%	
	Beginning monthly payment, including principal, interest, and mortgage insurance	$	
	Maximum monthly payment	$	
	Other important loan terms		
	Beginning loan balance	$	
	Maximum loan balance	$	
	Length of loan	years	
	Amount due at end of loan	$	
	Interest rate can rise as early as		
	Prepayment penalty: Maximum fee you pay if you pay off the loan early	$	
	Monthly escrow for taxes and insurance?	__ No	__ Yes
	Total settlement costs	$	

* The APR is the annual rate your credit will cost you. It combines the interest rate and fees charged. You should shop on the APR instead of the interest rate. The interest rate does not include the fees.

Appendix 2

NCLC MODEL GFE DETAILS FOR BROKER COMPENSATION

MORTGAGE BROKER COMPENSATION	
Mortgage Broker Fees paid by borrower directly (included in settlement charges):	$ ________
+additional fee received by broker from lender and paid by borrower through increased loan interest rate:	$ ________
Total Broker Fees:	**$ ________**

You could ask us for other loans. This loan was based on our payment of some fees to your broker or other closing costs. The table below shows how this loan compares to loans where we pay your broker more or less money.

	This loan	If we don't pay the broker	If we pay the broker more money
Loan amount	$	$	$
APR	%	%	%
Monthly payment	$	$	$
Maximum payment	$	$	$
How soon the interest rate can rise			
Maximum prepayment penalty	$	$	$
Maximum loan balance	$	$	$
Total settlement costs	$	$	$

NAMB
National Association of Mortgage Brokers

Prepared Testimony of

Marc Savitt, CRMS
President

National Association of Mortgage Brokers

On

"HUD's Proposed RESPA Rule"

Before the

Committee on Financial Services,

Subcommittee on Oversight & Investigations

United States House of Representatives

Tuesday, September 16, 2008

Good morning Chairman Watt, Ranking Member Miller, and Members of the Subcommittee, I am Marc Savitt, CRMS, President of the National Association of Mortgage Brokers ("NAMB"). Thank you for inviting NAMB to testify today on the Department of Housing & Urban Development's ("HUD") Proposed Real Estate Settlement Procedures Act ("RESPA") Rule. We appreciate the opportunity to discuss this issue, which is of vital importance both to consumers and to our members.

NAMB is the only national trade association exclusively devoted to representing the mortgage broker industry, and NAMB represents mortgage brokers in all 50 states and the District of Columbia. Our members are independent, small business men and women that adhere to a strict code of ethics and best lending practices[1] when taking consumers through the loan process. The business relationships that our

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[1]All mortgage originators who wish to be members of NAMB will be required to meet the Lending Integrity Seal of Approval® criteria as a requirement of membership by January 1, 2009. In order to use the Lending Integrity Seal, members must meet the following criteria: 1) must hold a valid state license/registration; 2) national criminal

members maintain with various lenders allow NAMB brokers to provide consumers with numerous financing options and to offer consumers some of the most competitive mortgage products available in the marketplace.

Once again, we would like to thank Chairman Watt and the members of the Subcommittee for their leadership and interest in HUD's Proposed RESPA Rule ("Proposed Rule"). NAMB commends this subcommittee for taking time to examine the Proposed Rule and its potential impact on consumers and our mortgage market.

I. Mortgage Brokers & the Current Market

A. The Role of Mortgage Brokers

A mortgage broker is a real estate financing professional or entity that works with both borrowers and lenders, while representing neither, to obtain a mortgage loan. A mortgage broker works with consumers throughout the complex mortgage origination process. Accordingly, a mortgage broker's role may include taking an application; performing a financial and credit evaluation; producing documents; working with realtors; ordering title searches, appraisals, and pay off letters; assisting in remedying faulty credit reports or title problems; and facilitating loan closings. The assistance a mortgage broker provides varies widely, depending on the nature of the transaction, the requirements of the customer, lender, or loan purchaser, and other factors.

A mortgage broker may have a working relationship with one or more banks or other lenders and may provide the consumer with access to a wide range of options for financing a home. This allows mortgage brokers to provide consumers a highly efficient and cost-effective means to obtain a mortgage that fits the consumer's financial goals and circumstances.

Mortgage brokers also facilitate competition in the marketplace and help drive costs down for borrowers. In fact, a 2005 independent study conducted by economists at three major universities concluded that "broker-originated mortgages are less costly to the borrower than lender-originated mortgages after holding other loan terms and borrower characteristics constant."[2] Similarly, a study by Richard Todd of the Federal Reserve Bank of Minneapolis and Professor Morris Kleiner of the University of Minnesota stated, "[b]rokers have helped to shorten the loan process and made it cheaper."[3] This study also showed that when certain state regulatory burdens were imposed on brokers that impeded brokers' entry into mortgage markets, the number of brokers declined, and those states experienced "higher foreclosure rates, and a greater percentage of high-interest-rate mortgages."[4]

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background check; 3) minimum of six (6) hours of professional education annually; minimum of two (2) hours of ethics training biennially; 4) three letters of reference or three professional references; 5) pledge to adhere to NAMB Code of Ethics and Professional Standards, *and* abide by NAMB's grievance review process and rulings.

[2] Amany El Anshasy (George Washington University), Gregory Ellihausen (Georgetown University) & Yoshiaki Shimazaki (Oklahoma State University), *The Pricing of Subprime Mortgages by Mortgage Brokers and Lenders*, July 2005 ("Mortgage Pricing Study"), at 12.

[3] Morris Kleiner & Richard Todd, *Mortgage Broker Regulations that Matter: Analyzing Earnings, Employment, and Outcomes for Consumers*, National Bureau of Economic Research Working Paper 13684 (December 2007)("Broker Regulations Analysis") at 7.

[4] Broker Regulations Analysis at 1.

B. Evolving Markets & The Converging Roles of Mortgage Originators

Mortgage markets have evolved rapidly in recent years, as have the roles of mortgage professionals and the entities with whom they are employed. Today, it is not uncommon for these individuals or entities to work in multiple capacities or to assume different roles in mortgage transactions.

In an analysis of mortgage broker regulations, Richard Todd and Professor Morris Kleiner noted, "the actual roles of brokers, loan officers, lenders, and others are not rigidly bound and often blur."[5] The Mortgage Bankers Association of America has also acknowledged this fact, stating recently that "Mortgage bankers sometimes function as mortgage brokers, offering the loan products of other, larger mortgage bankers."[6]

Accordingly, some state laws now expressly acknowledge that a single entity may be acting in multiple capacities – as both a lender and a broker. However, despite this shift in market realities and regulation in some states, the rules promulgated under RESPA have gone virtually unchanged since 1992.

Historically, mortgage brokers and mortgage lenders could be readily distinguished. Brokers did not lend money, and lenders did not serve as portals for competing providers of funds. However, in recent years, the lines between distribution channels have blurred, as the "originate to distribute" model of mortgage financing (where lenders promptly repackage and sell the loans they originate) has become commonplace.

In fact, it is now common for mortgage companies to act in multiple capacities. Even within a single transaction, the role in which a company may act may change during the application and processing functions from a lender to a broker, and back again, depending on circumstances. In addition, since HUD authorized affiliated business arrangements ("AfBAs"), many entities in the mortgage industry have established such relationships with developers, builders, real estate agents, and title companies, thus further confusing traditional roles and responsibilities.

Increasingly, mortgage bankers or lenders are functionally acting as a brokers because they often (i) enter into multiple contracts with various banks and lenders to offer an array of loan products, (ii) know at the time of closing that they have pre-sold or will quickly sell the loan, and (iii) generally know how much they will make off the loan when it is sold. Similarly, mortgage bankers and lenders sometimes operate as correspondent lenders by simply fronting mortgage funds for another bank, lender or the secondary market. As correspondent lenders, these entities are then compensated by the market, in addition to the consumer, for the temporary fronting of funds.

Conversely, we also see some brokers that act as mortgage bankers or lenders. For example, a broker may fund a loan by accessing a warehouse line of credit, and then promptly sell that loan to a purchaser who has previously committed to buy the loan.

Dramatic advances in technology have served to accelerate this convergence of the roles of mortgage originators. The introduction of automated underwriting, web-enabled credit scoring, and the ubiquity of computers have helped blur the distinctions between historically different functions. In fact, originators today tend to use the same software regardless of whether they are acting as broker or funding the loans they originate. The distinctions that still exist between mortgage originators are largely being determined by the click of a mouse.

[5] Broker Regulations Analysis, at 5, n.4.

[6] *Mortgage Bankers and Mortgage Brokers: Distinct Businesses Warranting Distinct Regulation,* Mortgage Bankers Association (May 2008), fn 9, at 13.

To the consumer, none of this is readily apparent. As the aforementioned 2005 university study observed, today "[b]orrowers may canvass mortgage originators without taking into account or even knowing whether an originator is a broker or lender."[7] Because consumers are largely unaware of, and indifferent to, the technical distinctions drawn between the originators with whom they are dealing, it is imperative that consumers be given the same information about the mortgage transaction regardless of the type of originator involved.

To serve consumers' interests effectively, regulatory initiatives relating to mortgage originators must address the mortgage market as it is today, not as it existed a generation ago. This means acknowledging the convergence of the roles of brokers, banks, and lenders; and applying rules equally to all of these originators.

Still, regulations implementing RESPA, and other provisions of applicable law drafted before the "originate to distribute" model became ubiquitous, retain vestigial distinctions between brokers and lenders that are no longer meaningful. These distinctions create market dysfunction which the Proposed Rule should seek to remedy, not exacerbate. Yet, in the Proposed Rule, lenders, unlike brokers, do not need to disclose what they are paid for originating loans that they do not retain for their own portfolios.

II. HUD's Proposed RESPA Rule & the Current Market

The Proposed Rule, published on March 14, 2008, seeks to simplify and improve the disclosure requirements for mortgage settlement costs under RESPA, and consequently, to protect consumers from unnecessarily high settlement costs. Accordingly, the Proposed Rule would, among other things, revise and standardize the Good Faith Estimate form ("GFE"), modify the HUD-1 Uniform Settlement Statement ("HUD-1"), impose additional disclosure requirements, require recitation of a "closing script" to borrowers, and clarify instructions as to how applicable forms are to be completed.

NAMB applauds HUD's response to problems in mortgage markets, and shares HUD's resolute commitment to protecting consumers from unnecessarily high settlement costs. NAMB believes that measures which target abusive practices and enhance transparency of the loan origination process benefit not only consumers, but also NAMB's members, who are already required to adhere to a professional code of ethics and best lending practices. In fact, for that reason, NAMB strongly supports numerous consumer protection measures in addition to those put forth in the Proposed Rule, including provisions which are beyond the jurisdiction of HUD and within the purview of other federal agencies or state regulators – including Title V of H.R. 3221 (Housing & Economic Recovery Act of 2008) implementing the new mortgage originator licensing and registration law, the Secure & Fair Enforcement Mortgage Licensing (S.A.F.E. Mortgage Licensing Act). All consumers deserve the same standard of professionalism, information and protection against fraud and abusive lending practices regardless of where they obtain their mortgage. To ensure all mortgage originators are well educated and knowledgeable about the loan products they offer, NAMB has long advocated for uniform licensure, education (including ethics training) and criminal background checks for each and every individual.

NAMB objects, however, to those components of the Proposed Rule that would not best serve the consumer and instead would move away from simplifying the settlement process for consumers and further confuse consumers. NAMB has concerns with numerous aspects of the Proposed Rule either because they would impede competition, treat direct competitors differently, fail to reflect the most authoritative research, or fail to consider the most effective and least burdensome alternatives.

[7] Mortgage Pricing Study at 8.

HUD proposes to make bold changes in the marketplace through implementation of the Proposed Rule. However, in light of the current market situation – rising home foreclosures, the credit crunch, the day-to -day changes to the marketplace and rapid Congressional and regulator response, among other factors – NAMB questions the appropriateness of the timing and implementation of the Proposed Rule.

Today's, mortgage market is significantly strained and continues to experience turmoil and change. The market has lost over 250 lenders, underwriting standards have tightened, minimum credit scores have increased and new rules have been implemented by the Federal Reserve Board. In addition, Congress continues to consider sweeping changes to how loans are originated in the United States. Before implementing sweeping changes to the settlement process, a thorough analysis should be undertaken to ensure any changes made to RESPA are done so with a positive impact on consumers and the industry that serves those consumers, not a negative impact.

At this time, NAMB believes HUD's efforts, and the mortgage market in general, may be better served by focusing on the many issues facing homeowners today and providing support for those consumers currently at risk of losing their home to foreclosure. NAMB believes HUD should continue to move forward in its RESPA reform process, but should do so in conjunction with the Federal Reserve Board in its review of Regulation Z and issue a new Proposed Rule. As regulators, Congress, and industry focus on the issues at-hand we must be cautious and ensure that the market has an opportunity to stabilize, accommodate changes, and provide the necessary assistance to borrowers facing foreclosure and in need of help from various refinancing programs administered by HUD.

III. Principles that should Guide Proposed Reforms

Any policy initiatives to be implemented by HUD or any other governmental entity must, above all else, meet two criteria.

First, the governmental entity must identify and articulate the proper policy goals. Those goals should be identified through a careful analysis of how consumers are currently served by mortgage markets, and by positing what systemic traits those markets should have to ensure that consumers' are best protected.

Second, the governmental entity must consider a full range of alternative means to achieve the articulated policy goals, and subject each of those possible alternatives to rigorous scrutiny to determine, based on all available studies and the most thorough empirical research, which alternative best achieves the policy objectives. In particular, the agency should carefully consider data and quantifiable evidence produced by other government agencies with particular expertise in the subject area or independent academic researches whose backgrounds permit them to make an informed and disinterested assessment of the relevant facts

As discussed herein, NAMB believes that the Proposed Rule implementing RESPA meets these two criteria in certain respects, but fails to do so in a number of other areas.

IV. Specific Proposals Negatively Impacting Mortgage Brokers & Consumers

A. Inequitable Disclosure of Yield Spread Premiums ("YSP")

YSP constitutes some portion of the compensation owed to a mortgage broker for the goods, services, and facilities provided when originating a loan transaction. The Proposed Rule reclassifies YSP as a credit to the borrower. The practical effect of this change is to put mortgage brokers at a competitive disadvantage by imposing asymmetrical disclosure obligations among originators receiving comparable compensation. Recharacterizing YSP as a credit to the borrower also invites gamesmanship by competing originators,

which may exacerbate rather than eliminate confusion among consumers when shopping for a mortgage loan. The Proposed Rule also would at times require the reported credit to be negative, a result which almost certainly would increase confusion among borrowers.

The Proposed Rule perpetuates the inequity between broker and lender transactions, as regulated under RESPA. Despite the fact that our mortgage market has evolved and originators' roles have converged under the "originate to distribute"[8] model, the Proposed Rule maintains, and even accentuates, an artificial difference between broker transactions (disclosure of YSP) and lender transactions (no disclosure of similar indirect compensation). As we have outlined in detail above, the era of clear differentiation between competitors in the mortgage market is over. The fact that this arbitrary distinction is perpetuated in the new GFE represents a fatal flaw in the Proposed Rule.

B. Proposal to Require Use of New GFE

The Proposed Rule states that, "[I]n order for the GFE to serve its intended purpose, which is to apprise borrowers of the charges that they are likely to incur at settlement, a number of specific changes to the GFE requirements are required to make it firmer and more useable. Accordingly, [the] proposed rule would establish a new required GFE form to be provided to borrowers by loan originators in all RESPA covered transactions." [9]

The Proposed Rule presents those changes in ten subcategories, each corresponding to different aspect of the revised GFE. Those subcategories, and NAMB's comments on each, are addressed below. As noted, NAMB supports the goals which the revised GFE is meant to serve. Also, NAMB supports certain elements of the revised GFE. However, NAMB does not support the revised GFE as set forth in the Proposed Rule.

Replacing a one page form with four pages does not facilitate consumer understanding. Moreover, some of the information included in the form, such as the unwarranted distinctions among mortgage originators, serves, as the Federal Trade Commission (FTC) has concluded, to confuse consumers and impede competition. Finally, some of the most crucial information for consumers is either not given sufficient emphasis, as with the explanation of the role of mortgage originators and importance of comparative shopping, or is not addressed at all, as with information about service release premiums (SRP) and payments created by AfBA relationships.

1. Changes to Facilitate Shopping

The Proposed Rule would bifurcate the application process by establishing a new definition for a "GFE application" and a separate new definition for "mortgage application."

The "GFE application" would be comprised of those items of information a borrower would submit to receive a GFE, including name, Social Security number, property address, gross monthly income, borrower's information on the house price or best estimate of the property value, and the amount of loan sought. The GFE application would provide the "trigger for initial RESPA disclosures," which, HUD asserts, could then be used to facilitate comparative shopping. The "mortgage application" would be submitted after the GFE application, once the borrower chooses to proceed with a particular loan originator. The mortgage application would ordinarily expand upon GFE application by providing such

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[8] Broker Regulations Analysis at 5, n.4.

[9] HUD, *Real Estate Settlement Procedures Act (RESPA): Proposed Rule to Simplify and Improve the Process of Obtaining Mortgages and Reduce Consumer Settlement Costs under the Real Estate Settlement Procedures Act*, 73 Fed. Reg. 14.030 (March 14, 2008)

information as bank and security accounts and asset and liability information. The credit decision would then be based on the more expansive information from the borrower. Nonetheless, the Proposed Rule expressly states that "borrowers may not be rejected unless the originator determines that there is a change in the borrower's eligibility based on final underwriting ...[or by] "unforeseeable circumstances."[10]

NAMB objects to the Proposed Rule's bifurcation of the application process. The new GFE application, as currently proposed, is unworkable.

Because the Proposed Rule does not present a GFE application form, parties seeking to comply with the Proposed Rule would have to rely solely on the text to determine what the GFE application would include and how it would be processed. The Proposed Rule specifies certain information that would be listed on the form, such as Social Security numbers and property addresses, but does not include certain key information, such as borrower assets and property appraisals, that would be critical to the lender's response. Also, the Proposed Rule does not provide needed guidance on such points as whether a GFE application would be required in all instances, whether it would be signed, and what would constitute "unforeseeable circumstances" sufficient to justify revising the terms specified in the GFE. Further, the Proposed Rule fails to explain how the GFE application and revised GFE would be coordinated with such other provisions of applicable law, such as Federal Reserve Board Regulations B, C, and Z. Nor does the Proposed Rule explain when redisclosure of a GFE application may be required or how that might work.

Perhaps most troubling, without a proposed form, there also has not been any of the testing which, as the Proposed Rule notes at great length elsewhere, is essential to development of sound policies and effective forms.

2. Addressing Up-Front Fees that Impede Shopping

The Proposed Rule would limit the fees that could be charged by a loan originator to provide a GFE to "the cost of providing the GFE, including the cost of an initial credit report."[11]

NAMB does not object to limiting the fees that could be charged to provide a GFE to the loan originator's costs in doing so. NAMB believes that, so long as regulatory impediments do not impede competition, the marketplace will tend to reduce those fees in most cases, perhaps even to zero. However, until the Proposed Rule is implemented, it is impossible to predict how burdensome this provision would prove to be, and how substantial the costs loan originators would be required to bear as a result. In view of that uncertainty, the Proposed Rule must provide loan originators with needed flexibility, particularly since GFEs—unlike, for example, the credit reports which applicable law requires be made available to consumers at no cost at least annually—may not be provided through automated means, and involve a very real commitment of time and resources to prepare.

3. Introductory Language

The Proposed Rule would add introductory language to the GFE that explains the interest rate, settlement charges, settlement date, and the timing required to lock in the interest rate. In addition, the Proposed Rule would add language at the end of the GFE (though it is discussed in the subsection of the Proposed Rule relating to "Introductory Language"), which advises consumers that "Only you can shop for the best loan for you. Compare this GFE with other loan offers, so you can find the best loan."[12]

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[10] Id. at 14,035-36.
[11] Id. at 14,036.
[12] Id. at 14,036, 14,095-97.

NAMB believes that the introductory language set forth by the Proposed Rule, as well as the language encouraging comparative shopping proposed at the end of the revised GFE, is either inaccurate or inadequate and should be improved.

The Proposed Rule would revise the introductory language of the GFE to read, "The interest rate for this GFE will be available until ____." Yet it is potentially misleading to suggest that a borrower will receive a specific interest rate prior to final application. A more accurate alternative would be to state, "The interest rate quoted on this GFE is ___. This rate is not guaranteed. Until it is locked, this rate will float with the market and can change without notice." It is very important that the consumer understand that fact. Failure to do so will lead to confusion about what is, in many cases, the single most important economic attribute of the loan—the interest rate. NAMB strongly supports revising the GFE to encourage comparative shopping. In general, NAMB believes that the better informed consumers are, the more likely they are to make a more sound financial decision. However, as currently drafted, the revised GFE appended to the Proposed Rule would foster less understanding of the loan origination process, not more.

The language encouraging comparative shopping is also inaccurate in that it incorrectly characterizes the GFE as a "loan offer." That is misleading. The proscribed text leaves borrowers with the impression that they have been approved; they have not. As the Proposed Rule itself notes, a credit decision, and thus a loan offer, cannot be made until a mortgage application is received and processed. Thus, that reference should be changed to "other estimates."

In addition, the language encouraging comparative shopping should be made even more conspicuous, more emphatic, and more informative. Specifically, NAMB strongly encourages HUD to adapt language developed by the FTC based on extensive testing on consumers.

As noted, over the course of several years, the FTC conducted research into the efficacy of proposed disclosures and their effect on consumer decisions and market outcomes. The FTC has presented its findings in two separate reports totaling over 400 pages. In addition, those reports specifically address the asymmetrical disclosure obligations imposed upon brokers, but not other originators performing similar functions and being paid similar compensation. The prototype disclosure forms developed by the FTC include prominent legends in large typeface which expressly advise borrowers that mortgage originators, including both brokers and lenders, do not represent borrowers, and thus the "lender or broker providing this loan is not necessarily shopping on your behalf or providing you with the lowest cost loan." The legend also encourages borrowers, in all caps, to "COMPARISON SHOP TO FIND THE BEST DEAL." [13] FTC testing showed that consumers got the message.

NAMB strongly urges HUD to adopt the FTC prototype disclosure forms instead of implementing the Proposed Rule's provisions on broker compensation. If the FTC forms are not adopted in their entirety, NAMB also suggests that the FTC language be incorporated earlier in the form, and in a more prominent typeface, than the language at the end of the proposed GFE addressing comparative shopping. The FTC forms have been thoroughly tested, and they are more effective means of addressing the policy concerns raised by the Proposed Rule. Also, as the FTC has explained, the prototype forms do not create anti-broker bias that can impede competition and lead consumers to make choices that are not in their best interests.

4. Terms of the GFE (Summary of Loan Details)

[13] 2007 FTC Study at H-13.

The Proposed Rule would provide that the revised GFE include a summary of the key terms of the loan, including the initial loan amount, the loan term, the initial interest rate, the initial monthly payment, and the rate lock period.[14]

NAMB supports inclusion of the loan details identified by the Proposed Rule in the GFE. In addition, NAMB believes that consumers would be well served by the inclusion of certain additional monthly expenses specific to the property, such as homeowners' association dues, if applicable.

5. Period During Which the GFE Terms are Available to the Borrower

The Proposed Rule would provide that the interest rate stated on the GFE would be available until a date set by the loan originator. The estimate of the charges for all other settlement services would be available for at least ten business days. [15]

As noted, NAMB believes that it is meaningless, and potentially misleading, to suggest that a borrower would receive a specific interest rate prior to final application. As a consequence, NAMB suggests more specific language making it clear that the quoted rate may change until locked.

The "ten business day" period during which estimated settlement charges would be available is too long. Ten "calendar days" would be more reasonable, and would conform more closely to market realities.

6. Consolidating Major Categories on the GFE

Under current RESPA rules, the GFE simply lists estimated charges or ranges of charges for settlement services. The Proposed Rule would group and consolidate all fees and charges into major settlement cost categories, with a single total amount estimated for each category. [16]

NAMB objects to consolidating major categories of the GFE. Such categories tend to lead to confusion, not clarity, as components are not evident to consumers until presented with the HUD-1, in which they are disclosed separately.

RESPA now requires, under Part 3500, Appendix D, a special form for payments by a referring party to a settlement service provider involved with an Affiliated Business Arrangement. This disclosure statement must be made in writing at or before the time of the referral and must be acknowledged by the mortgage applicant. This disclosure includes the name of the provider of the settlement service and the charge or range of charges. It also delineates between those items that may not be required by the originator and those that may be required. This form contemplates the name and amount of charges the applicant will pay. This existing form is in direct conflict with the new GFE as proposed. By eliminating the disclosure of the name of the provider on the GFE, it renders this important consumer protection form useless. By grouping certain charges into categories, some of the charges on this document are now combined with other amounts that are not covered under the AfBA disclosure. Only confusion can be the result of creating cost groupings and not amending the required disclosure under Part 3500, Appendix D. It will also make it impossible for the consumer to shop settlement service providers who are not affiliated. NAMB believes that consumers will lose this important consumer protection (choice of provider and prohibiting required use) and will be confused by such a change. At the very least, HUD should formally address this issue and consumer test the combination of the new GFE with the existing AfBA form to determine what such a change will bring to the marketplace.

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[14] 73 Fed. Reg. at 14,036.
[15] Id. at 14,037.
[16] Id.

Regulation X under RESPA, Section 3500.7 also requires a disclosure if a particular provider is required (Section 3500.2) by the lender (other than the lender's own employees). This disclosure must state that the provider is required to give the name, address, and phone number of each provider, and describe the nature of any relationship between such provider and the lender. NAMB believes that this is an important consumer protection that should be maintained. Required use, in any form, gives rise to the possibility of higher prices to the consumer and eliminates the possibility of the consumer shopping for such service or rejecting the lender's loan offer. By eliminating the detail on the GFE as proposed, the requirements under this section of RESPA are rendered confusing at best and harmful at worst. Some of these charges will naturally be grouped under the new GFE as proposed, thereby eliminating the detail on that form, only to have a different form executed by the consumer which includes certain items but not others. How is a consumer to determine the appropriateness of a charge when it is grouped on one form and itemized on another? How is a consumer to determine the nature of the relationship? Additionally, the consumer has no way to compare the detailed costs on this form versus the grouped costs on the proposed GFE. NAMB believes that consumers will lose this important consumer protection and will be confused by such a change. At the very least, HUD should formally address this issue and consumer test the combination of the new GFE with the existing 'Particular Providers' form to determine what such a change will bring to the marketplace.

NAMB recommends that the reference to charges for "services" not be used on the proposed GFE with respect to originators. Use of that term presents a potential conflict with state law, as some states expressly prohibit originators from imposing a "service charge," and presents state tax concerns due to current and contemplated state taxes on "services." Use of the term also presents a concern relating to federal tax code provisions that allow consumers to deduct broker origination fees. Characterizing such fees as a "service charge" could affect their deductibility under Internal Revenue Service ("IRS") regulations. A possible alternative could be "origination charges," which would also correspond to the reference to "Adjusted Origination Charges."

NAMB also recommends that the GFE include the names of service providers selected by the loan originator to facilitate comparative shopping.

In addition, NAMB notes that the RESPA statute expressly provides for the disclosure of a "range" of settlement charges and fees. [17] Accordingly, NAMB questions whether HUD, whose regulations must be consistent with the authorizing statute, has the authority to pronounce that loan originators who disclose a range of charges and fees do not comply with RESPA.

7. Option to Pay Settlement Costs

The revised GFE appended to the Proposed Rule would include a statement advising the borrower how the interest rate of the loan affects the borrower's settlement costs, and include actual available options in that regard on the GFE form.

NAMB strongly supports inclusion of information regarding the relationship between closing costs and interest rates on the proposed GFE. Understanding of that relationship is central to understanding loan pricing, originator compensation, and other basic economic elements of the mortgage process.

8. Establishing Meaningful Standards for GFEs

[17] 12 U.S.C. § 2601.

The Proposed Rule would prohibit costs for originators' service charges, adjusted origination charges, locked interest rates, and government recording and transfer charges that are charged at closing from exceeding the estimates for those costs listed on the GFE "absent unforeseeable circumstances." In addition, the Proposed Rule would prohibit the sum of all other services from increasing at settlement more than ten percent "absent unforeseeable circumstances."

NAMB supports the proposal to limit increases in costs disclosed on the GFE that are later assessed at closing. However, further guidance is needed as to what constitutes "unforeseeable circumstances," including specific and detailed examples so that parties seeking to comply have reasonable assurance that they do so.

9. Important Information for Borrowers

The Proposed Rule would include in the revised GFE information for borrowers that, HUD asserts, would enhance their understanding about the process of obtaining a mortgage loan. That information, which would be listed on the fourth and final page of the GFE, would address: the financial responsibilities of homeowners, how to apply for the loan described on the GFE, how to obtain more information, how to use the shopping chart, and the consequences of any sale of the mortgage loan.

NAMB generally supports the inclusion of the information listed on page four of the proposed GFE. However, NAMB believes that the information relating to the consequences of any sale of the mortgage loan, which are described in small print at the very end of the form, merits greater emphasis and more detail. Specifically, NAMB proposes that the description of the additional compensation to lenders which would occur upon sale of the loan should be moved to block two on page two of the proposed form, where it should appear beneath the check box stating "The credit or charge for the interest rate you have chosen is included in our 'service charge'." SRPs are, like YSPs, a form of compensation, and should be identified as such to the borrower in a place and in a manner which facilitates the consumer's understanding of the similarities between the two.

More fundamentally, as discussed in detail below, NAMB strongly advocates ensuring that the GFE, HUD-1, and any other documents developed by HUD under RESPA impose symmetrical disclosure obligations on all mortgage loan originators. Failure to do so would deprive consumers of important information, and compromise their economic interests by impeding competition among originators.

10. Enforcement

The Proposed Rule provides that charging a fee in excess of the tolerance, or any other failure to follow the GFE requirements, constitutes a violation of Section 5 of RESPA.

NAMB supports the Proposed Rule's enforcement provisions, provided both that NAMB's suggested changes to the GFE form are implemented, and that HUD adopt a provision currently under consideration that would allow loan originators a limited period of time to remedy any potential violations of the tolerances set forth in the Proposed Rule.

C. Lack of Authority

The Proposed Rule fails to cite any authority in support of its characterizations of broker conduct, and fails to propose policies which would address that conduct if it existed.

In rationalizing HUD's position with respect to the disclosure of YSPs, the Proposed Rule states,

> [M]any brokers hold themselves out as shopping among the various funding sources for the best loan for the borrower, and do not explain to the borrower that the payment they receive from the lender is derived from the borrower's interest rate. Some may even assert that the YSP is not a payment the borrower needs to be concerned with.[18]

Not a single citation is offered in support of these accusations. In the recent case of AmeriDream v. Jackson, the Federal District Court for the District of Columbia took the extraordinary step of voiding a HUD regulation because, among other grounds, the regulation was based on "flimsy anecdotal evidence." [19] The assertion in the Proposed Rule about the conduct of mortgage brokers is worse: it is based on no evidence at all.

Rather than impugning brokers, a more constructive approach would be for HUD to examine current law and industry practice to determine what provisions are currently in place to ensure that borrowers fully understand the relationship of loan originators to the borrower, the importance of comparative shopping, and the interplay between mortgage rates, originator compensation, and closing costs, and assess how those provisions might be strengthened.

In fact, federal and state law, as well as NAMB policies, already direct that mortgage brokers make it very clear that the broker is acting as an independent agent and not necessarily acting to obtain the best loan for the borrower.

For example, when a prospective homebuyer applies for a loan, they are provided with a document drafted by HUD, Buying Your Home: Settlement Costs and Helpful Information.[20] That pamphlet advises borrowers, in bold-face type, that "A mortgage broker may operate as an independent business and may not be operating as your 'agent' or representative."[21] Accordingly, HUD further advises borrowers, "Your mortgage broker may be paid by the lender, you as the borrower or both."[22] The Proposed Rule makes no mention of this information which HUD already provides to every prospective borrower, does not explain why the current disclosure is inadequate, and does not identify any basis for concluding that borrowers will pay more heed to that information if simply presented in another form. To the contrary, the Proposed Rule presumes, without citing any source as a basis for that presumption, that borrowers mistakenly view brokers as acting in a capacity which HUD already advises borrowers is not the case.

In addition to current HUD disclosures, NAMB itself has developed a more detailed disclosure document describing the role of mortgage originators, the use of which has been mandated by several states and the District of Columbia. NAMB believes this form should be required nationally.

In the late 1990s, NAMB developed that disclosure form, or Mortgage Loan Origination Agreement ("Agreement), to be given to a prospective borrower before application. That form, which is very widely used today as a supplement to the GFE and HUD-1 disclosure forms, expressly states that the broker does not represent the borrower and is not obligated to obtain the best deal.

The Agreement is simple and direct, consisting of only two short paragraphs, one describing the nature of the broker relationship and one explaining how brokers are compensated. Furthermore, the Agreement is typically presented to the consumer for review even before making the loan application; a signed copy of

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[18] Id. at 14,042. (Emphasis added.)
[19] *AmeriDream v. Jackson*, Civil Action No. 07-1752 (PLF)(D.D.C. 2008) at 18.
[20] U.S. Dep't of Hous. & Urban Dev., *Buying Your Home: Settlement Costs and Helpful Information* (June 1997)
[21] Id. at 4.
[22] Id. at 4.

the Agreement is among the materials required to initiate the application process. The operative portion of the Agreement paragraph states in its entirety:

> **Section 1. Nature of Relationship**
> In connection with this mortgage loan we are acting as an independent contractor and not as your agent. We will enter into separate independent contractor agreements with various lenders. While we seek to assist you in meeting your financial needs, we do not distribute the products of all lenders or investors in the market and cannot guarantee the lowest price or best terms available in the market.
>
> **Section 2. Our Compensation**
> The lenders whose loan products we distribute generally provide their loan products to us at a wholesale rate. The retail price we offer you—your interest rate, total points, and fees—will include our compensation. In some cases, we may be paid all of our compensation by either you or the lender. Alternatively, we may be paid a portion of our compensation by both you and the lender. For example, in some cases, if you would rather pay less up-front, you may be able to pay some or all of our compensation indirectly through a higher interest rate in which case we will be paid directly by the lender. We may also be paid by the lender based on (i) the value of the loan or related servicing rights in the market place or (ii) other services, goods or facilities performed or provided by us to the lender.[23]

In addition to the disclosures currently mandated by applicable law or industry practice, NAMB strongly supports still more disclosures to that effect, such as that proposed by the FTC, which describe the relationship of loan originators to the borrower, highlight the importance of comparative shopping, notify the borrowers that they are the only ones who can conduct that comparative shopping on their own behalf, and explain the interplay between mortgage rates, originator compensation, and closing costs.

For example, NAMB supports enhancing the language noted in small type at the top of page three of the proposed GFE regarding comparative shopping, as well as the language in small type at the very end of the proposed GFE regarding the fees that may be received by a mortgage originator upon a subsequent sale of the loan. Specifically, NAMB supports addressing the issues of comparative shopping and originator compensation together. Highlighting the sources of originator compensation – that is, that it may come in whole or in part from lenders – underscores the importance of a borrower comparison shopping on his or her own behalf. In addition, because that point is so critical for a consumer to understand, NAMB supports making it much more prominently and emphatically in the document.

Towards that end, NAMB strongly recommends that HUD adapt the text of the disclosure that the FTC developed based on extensive testing of how to promote informed decision making among prospective borrowers.

Like most good ideas, the FTC's proposal is simple. In essence, it would mandate disclosure of the Agreement in a more condensed and emphatic form. The FTC proposal would include a legend in the disclosure form that states, in large block letters, "HOW TO PROTECT YOURSELF." Beneath that is the statement "COMPARISON SHOP TO FIND THE BEST DEAL—The lender or broker providing this loan is not necessarily shopping on your behalf or providing you with the lowest cost loan."[24] The FTC found that consumers got the message: the efficacy of that alternative solution was confirmed by

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[23] Id.

[24] 2007 FTC Study at H-13.

empirical testing. In addition, because the FTC language acknowledged the similar roles of all mortgage originators, it did not impede the competition among originators that serves consumers well.

Although the Proposed Rule, without citing any authority for the statement, singles out mortgage brokers and claims they hold themselves out as shopping for the best loan for the borrower, the leading study on that point demonstrated that borrowers view both brokers and lenders as providing such assistance. As a consequence, any policy initiative meant to dispel that misconception should address all originators.

D. Inadequate Consideration of Empirical Data & Flawed Methodology

Exhaustive studies of mortgage disclosures by the FTC, the government's principal consumer protection agency, in 2004 and 2007[25] show that additional disclosures of mortgage broker compensation create confusion, cause consumers to choose more expensive loans, lead to a bias against mortgage broker transactions, and impede competition, thus hurting consumers.

Similarly, a 2008 study commissioned by the Board of Governors of the Federal Reserve concluded that upfront disclosures which single-out mortgage broker compensation may bias consumers against working with mortgage brokers and lead consumers to believe they will always pay less commission when working with a direct lender.[26]

Finally, in April 2007, the Joint Center for Housing Study at Harvard University released a 75 page report ("Harvard Mortgage Markets Study") which detailed the similarities between different loan originators, including the way both brokers and loan officers are compensated, along with the common consumer protection concerns each origination channel presents. Among the key recommendations presented in this report was a call for federal regulators to "establish minimum standards and apply rules equally to the marketplace," and to "create effective and adequately funded enforcement strategies to ensure that all mortgage brokers, loan officers, and mortgage originators play by the same rules."[27]

One of the Harvard Mortgage Markets Study's two authors, Ren Essene, echoed these points at a June 14, 2007 Federal Reserve Board hearing on the Home Equity Lending Market, stating:

> Fundamental fairness suggests that the nature and extent of federal oversight and consumer protection should not depend on the details of which particular mortgage broker or loan officer takes the mortgage application, which particular retailer or wholesaler originates the mortgage, and which secondary market channel is tapped to secure the investment dollars that ultimately funds the loan.[28]

Neither the Harvard Mortgage Markets Study nor Ren Essene's testimony is discussed, or cited, by the Proposed Rule. Moreover the Proposed Rule fails to give proper consideration to much of the other

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[25] James M. Lacko & Janis K. Pappalardo, The Effect of Mortgage Broker Compensation Disclosures on Consumers and Competition: A Controlled Experiment (2004)("2004 FTC Study"); James M. Lacko & Janis K. Pappalardo, Improving Consumer Mortgage Disclosures: An Empirical Assessment of Current and Prototype Disclosure Forms (2007)("2007 FTC Study").

[26] *See attached,* Macro International, Consumer Testing of Mortgage Broker Disclosures (July, 2008)("Broker Disclosure Study").

[27] Ren Essene & William Apgar, Understanding Mortgage Market Behavior: Creating Good Mortgage Options for All Americans, Joint Center for Housing Studies, Harvard University (2007)("Harvard Mortgage Markets Study")at vi.

[28] Testimony of Ren Essene, Research Analyst, Joint Center for Housing Studies at Harvard University, Before the Board of Governors of the Federal Reserve System Hearing On the Home Equity Lending Market (June 14, 2007) http://www.federalreserve.gov/SECRS/2007/August/20070823/OP-1288/OP-1288_90_1.pdf, at 8.

relevant and authoritative research conducted by the FTC, the Federal Reserve Board, and university scholars at a number of institutions.

Instead, the Proposed Rule relies exclusively on flawed methodology to assess the efficacy of revised disclosures relating to mortgage broker compensation. The HUD contractor that conducted the studies cited in the Proposed Rule failed to test the disclosures in actual transactions involving competing originators. The HUD contractor also failed to test consumer understanding of loan terms and consumers' ability to effectively comparison shop when YSP was not disclosed. Instead, the HUD contractor *assumed* the answer to the most fundamental question, which is, whether YSP disclosure aides consumer understand and comparison shopping.

Without empirical evidence to support the hypothesis, HUD conducted tests under the assumption that it is beneficial to consumers if YSP is disclosed. Therefore HUD's tests focused only on how, not whether, to disclose YSP. Similarly, HUD concluded, *without testing*, that there would not be a benefit to consumers if indirect lender compensation were to be disclosed in the same manner as YSP. As a result, HUD tested only the disclosure of indirect broker compensation.

E. Proposal to Modify the HUD-1 Settlement Statement.

The Proposed Rule would modify the current HUD-1/1A Settlement Statements to allow the borrower to compare easily specific charges at closing with the estimated charges listed on the GFE. In addition, an addendum would be added to the HUD-1/1A that would compare the loan terms and settlement charges estimated on the GFE to the final charges on the HUD-1 and would describe in detail the loan terms for the specific mortgage loan and related settlement information. The settlement agent would be required to read the addendum aloud to the borrower at settlement and provide a copy of it at settlement.

NAMB believes that the HUD-1 and GFE should mirror each other and promote clarity, understanding, and ease of use for consumers. However, because the proposed GFE, at four pages, is less user-friendly than the current version, mirroring the HUD-1 after the proposed document will not make it easier for consumers to understand and use.

F. The Closing Script

NAMB opposes the closing script. The closing script is certain to increase costs for consumers and lower the number of loans that can be closed in a day. NAMB estimates that the additional time and resources which would be consumed by implementing the closing script would average approximately $500 per loan, with no commensurate, or even discernible, benefit to consumers in light of disclosures already mandated. The closing script also presents practical and legal concerns. As a practical matter, loan closings would be further delayed, which in turn would make locking in loan terms more problematic. Also, the closing script would require the closing agent to assume an advisory role, particularly when the borrower asks questions, which may trigger state regulatory and licensing requirements. Also, the closing script would present issues relating to allocating responsibilities—and liabilities—among professionals involved with the loan.

G. Harmonization of HUD's Proposed RESPA Rule with the Federal Reserve's Truth In Lending (TILA) Rule

As the Proposed Rule notes, the Federal Reserve Board proposed new regulations under TILA relating to disclosure. Those proposed regulations were issued on January 8, 2008[29] and finalized on July 30, 2008.[30]

The Federal Reserve Board's (Board) Proposed Rule addressed the YSP in a manner that was, admittedly so, confusing to the consumer and reduced competition in the marketplace. In our comment letter, NAMB stated that the manner in which the Board was requiring such disclosure of the YSP was confusing to the consumer. NAMB explained that by applying such disclosures to mortgage brokers but not to creditors' employees who originate loans, would reduce competition in the market and harm consumers. NAMB explained that disclosing a broker's compensation would cause consumers to believe, erroneously, that a loan arranged by a broker would cost more than a loan originated by a loan officer. The FTC commented and cited its published report of consumer testing on mortgage broker compensation disclosures, and stated that focusing consumers' attention on the amount of the broker's compensation could confuse consumers and, under some circumstances, lead them to select a more expensive loan. The Board considered these comments, conducted consumer testing and withdrew the proposal relating to YSP. In its final rule, the Board stated it is "concerned that the proposed agreement and disclosures would confuse consumers and undermine their decision-making rather than improve it." [31] The Board recognized that such disclosure of the YSP, as proposed, would not serve in the consumers' interest and in fact, would further confuse the consumer. HUD's Proposed RESPA rule requires disclosure of the YSP that will produce the same or a similar result as the Board's proposed YSP disclosure.

The Board stated that they will "continue to explore available options to address potential unfairness associated with originator compensation arrangements such as YSP. As the Board comprehensively reviews Regulation Z, it will continue to consider whether disclosures or other approaches could effectively remedy this potential unfairness without imposing unintended consequences."[32] NAMB believes HUD, at a minimum, should take the same approach with its RESPA rule.

HUD's Proposed Rule states, "As HUD moves forward to finalize this rule, it will continue to work with the Board to make the respective rules consistent, comprehensive, and complementary."[33] Noting that intention, however, is of no consequence. Just as the Proposed Rule must explain how it relates to existing law, it must explain how it relates to the Board's amendments to Regulation Z. The Administrative Procedures Act (APA) requires as much, as does sound rulemaking.

The Proposed Rule also does not address the Risk-Based Pricing regulations[34] the Federal Reserve Board and FTC recently proposed pursuant to the "Fair and Accurate Credit Transactions Act of 2003," or "FACT Act."[35]

The FACT Act, which amended the Fair Credit Reporting Act ("FCRA"), created a new disclosure requirement – the Risk-Based Pricing Notice ("RBP"). The RBP must be given to the consumer when the credit report affects pricing or other terms of the credit product. Specifically, the statute says that the RBP must be given to a consumer when credit is extended on "material terms that are materially less favorable than the most favorable terms available" to a "substantial proportion" of that creditor's other

[29] Federal Reserve, Proposed Rule Amending Regulation Z, Implementing the Truth In Lending Act and Home Ownership and Equity Protection Act 73 Fed. Reg. 1,672.
[30] Federal Reserve, Final Rule Amending Regulation Z, Implementing the Truth In Lending Act and Home Ownership and Equity Protection Act, 73 Fed, Reg. 44,522.
[31] 73 Fed. Reg. at 44,563.
[32] 73 Fed. Reg. at 44,565.
[33] 73 Fed. Reg. at 14,034.
[34] Federal Reserve Board and FTC, *Fair Credit Reporting Risk-Based Pricing Regulations*, 73 Fed. Reg. 28,966 (May 19, 2008).
[35] Public Law 108-159.

customers. The notice may generally be provided at application, communication of an offer of credit, or when the credit is granted (closing for real estate transactions), which would allow lenders and brokers to provide a generic notice to all applicants at the time of application. But the FACT Act allows the Federal Reserve Board and FTC to specify the timing of providing the notice after the credit report has been used to set the rates and terms of the offer, thereby making the notice much more consumer-specific. Those requirements could affect RESPA regulations in numerous ways, none of which are addressed by the Proposed Rule. It is essential that the Proposed Rule assess their impact before finalizing still more mandated disclosures.

HUD should seek public comments on the interaction between its proposal, the final amendments to Regulation Z and the pending RBP regulations. HUD should also work with the Board as it considers additional disclosures pursuant to Regulation Z. Further, input from the parties who must comply with, and hope to benefit from, HUD's Proposed Rule is certain to improve any final regulation.

H. Administrative Procedures Act Compliance

The rulemaking process by federal agencies, including HUD, is governed by the APA, which sets forth clear standards which any proposed rulemaking must meet. In its current form, the Proposed Rule fails to comply with some of the most critical APA standards. Moreover, because of the materiality of those shortcomings, they may not be remedied in the final rule. At a minimum, the APA concerns relating to the Proposed Rule require the rule to be proposed again in a form which satisfactorily addresses those concerns, and which permits the public to comment upon changes and additions to the Proposed Rule's rationales and supporting materials.

The animating principles of the APA are relatively straight-forward: an agency may not abuse its authority by acting either arbitrarily or unilaterally. Although agencies develop regulations pursuant to statutory authority, they nonetheless may only act after articulating an adequate rationale for the proposed action, and identifying any data, studies, or analyses supporting the proposed policy course. Moreover, that rationale and supporting authorities must be presented to the public, which must be given an opportunity to comment on the Proposed Rule and its premises. In short, an agency may not simply assert that a regulation is in the public interest, it must demonstrate that the regulation is so, and it must afford the public it presumes to serve the right to examine and challenge the rule's premises.

Under the APA, if the final rule is not adequately justified by the rationale articulated by the issuing agency, if that rationale is not properly supported by the facts and data presented, or if the facts and data are not timely presented to the public to permit comment prior to adoption of a final rule, that rule is not valid. As the U.S. Circuit Court for the District of Columbia made clear in Association of Data Processing Service Organizations, Inc. v. Board of Governors of the Federal Reserve System, Section 706(2)(A) of the APA "enable[s] the courts to strike down, as arbitrary, agency action that is devoid of needed factual support."[36]

V. Recommendations

NAMB urges HUD to adopted recommended changes stated herein. NAMB urges HUD to conduct further research into the operation of modern mortgage markets and the efficacy of proposed disclosures, taking into account not only how YSP should be disclosed, but whether it should be disclosed, along with whether and how other forms of indirect originator compensation might be effectively disclosed. In

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[36] *Ass'n of Data Processing Svc. Orgs., Inc. v. Bd. of Govs. of Fed. Reserve System*, 745 F.2d 677, 683 (D.C. Cir. 1984).

conducting this research, NAMB strongly encourages HUD to give proper consideration to key studies in the field, such as those mentioned above.

HUD should also undertake new testing of any proposed disclosures, which both assesses how the forms would be used by actual mortgage originators, and how they would be received by actual borrowers in real transactions. Ultimately, we believe that new and comprehensive testing will further illustrate the need to amend the Proposed Rule and modify the GFE so there is equal disclosure of YSP and the similar compensation that lenders pay to their own sales staff.

Policies and promulgated rules that accentuate and perpetuate an artificial distinction between mortgage brokers and their direct competitors will only serve to impede competition, limit consumer choice, increase retail pricing, and ultimately hurt consumers.

VI. Conclusion

NAMB has strongly and repeatedly urged HUD to modify the GFE so that consumers understand the disclosures they are reading, to ensure that direct competitors are treated the same and that the artificial distinctions which still exit in mortgage transactions covered by RESPA disappear.

Today, we ask the members of this subcommittee to join us in calling upon HUD to: (1) refrain from publishing a final rule until the market has had ample opportunity to absorb and adjust to the changes and turmoil it has already endured; (2) focus immediate attention on helping borrowers in distress refinance through HUD-administered programs and avoid foreclosure; (3) revise the GFE, giving proper consideration and weight to the numerous studies calling for clarification of the disclosures and uniformity of disclosure across all distributions channels; (4) field test any prototype disclosure, with real consumers, prior to implementation; and (5) work in conjunction with the Federal Reserve to harmonize HUD's RESPA Proposal with the disclosures pursuant to Regulation Z.

NAMB strongly supports measures which empower consumers to make informed decisions to select a mortgage product based upon their own assessment of the comparative price, most appropriate product, and highest quality of service.

Again, thank you for the opportunity to appear before this subcommittee today to discuss this important issue. I am happy to answer any questions that you may have.

Written Statement

of

David H. Stevens
President of Affiliated Businesses
Long and Foster Companies

On Behalf of

The Real Estate Services Providers Council, Inc. (RESPRO®)

Before the
U.S. House of Representatives
Subcommittee on Oversight and Investigations
of the
Committee on Financial Services

On

The Department of Housing and Urban Development's (HUD) Proposed
Real Estate Settlement Procedures Act (RESPA) Rule

September 16, 2008

Good morning, Mr. Chairman and Members of the Subcommittee. My name is David H. Stevens and I am President of Affiliated Businesses for Long and Foster Companies.

Long and Foster Companies is the third largest residential real estate brokerage firm in the nation, with over 200 residential real estate brokerage offices that engage in real estate sales and leasing in Virginia, Washington, D.C., Maryland, West Virginia, Delaware, Pennsylvania, North Carolina, and New Jersey.

Long and Foster offers a full array of mortgage services through Prosperity Mortgage, which is a joint venture co-owned by Long and Foster and Wells Fargo Home Mortgage. In addition, we operate an independent mortgage banking firm, Walker Jackson Mortgage, in southeastern states from Florida to North Carolina. We also offer personal, commercial, and financial insurance protection from over 50 insurance companies through Long and Foster Insurance, a wholly-owned insurance agency. Another wholly-owned company, Mid-States Title, runs several joint ventures that conducted over 27,000 settlements last year.

Today I am representing the Real Estate Services Providers Council, Inc. (RESPRO®), a national non-profit trade association of over 200 residential real estate brokerage, mortgage, home building, title, and other settlement service companies who promote an environment that enables providers to offer diversified services for home buyers – often called one-stop shopping -- through affiliations, joint ventures, and other strategic alliances across industry lines.[1]

I. Overall Position of RESPRO® on HUD's Proposed RESPA Reform Rule

Because Long and Foster offers real estate brokerage, mortgages, title and closing services, and insurance, we share along with other RESPRO® members many of the concerns that my fellow witnesses are expressing in their testimony today over the potential impact of HUD's proposed RESPA rule on these individual industries. We support HUD's goal of providing simplified mortgage disclosures that make it easier for consumers to shop when they purchase or refinance a home. However, we believe that the rule it proposed on March 14, 2008 would have the opposite effect. For example:

[1] See Attachment 1 or http://www.respro.org/content.cfm?L1=1.0&L2=3.0 for membership list).

- The proposed Good Faith Estimate (GFE) is lengthy, complex, and cannot be easily compared by a borrower with the HUD-1 Settlement Statement at closing to determine whether the actual costs exceed the estimate provided at the time of the loan application.

- The proposed GFE contains terminology that conflicts with other disclosures consumers receive under the Truth in Lending Act (TILA) and the Equal Credit Opportunity Act (ECOA), which will add to the borrower's confusion during the loan application process.

- HUD's proposed new GFE and mortgage application process would overlap and conflict with the broader federal mortgage regulatory framework under TILA and ECOA, which would further add to the borrower's confusion.

- HUD proposed that closing agents be required to prepare and read a new "closing script" that even it estimates would take 45 minutes to read and would cost the consumer an additional $54 per closing. The closing script would also violate many state "unauthorized practice of law restrictions", and HUD did not anticipate how it would be delivered in non-face-to-face transactions or in transactions involving foreign languages.

These are just a few reasons why we believe HUD's 2008 proposed RESPA reform rule -- which was almost 100 printed *Federal Register* pages -- was fundamentally flawed. Given the short timetable for public comments (March 14 – June 13, 2008), the thousands of comments received, and the extremely short time after the deadline for comments that HUD took to analyze them, draft a final rule, and send it to OMB (June 13 – August 14, 2008), we think that it is extremely unlikely that HUD has modified the proposed rule in a manner that would resolve these and numerous other potential problems.

II. The Impact of the Proposed RESPA Rule on Diversified Real Estate Brokerage Companies and Their Customers

I am here today; however, to address the particular impact that the proposed rule would have on diversified real estate brokerage firms like Long and Foster Companies and our customers.

A. An Overview of Diversified Real Estate Brokerage Firms

The segment of the industry that I represent today is not insubstantial. According to the independent real estate research firm REALTrends, Inc., 285 of the nation's 500 largest residential real estate brokerage firms -- which were involved in 30% of all home purchase transactions in 2007 -- offer mortgages, and 240 of the top 500 firms offer title, closing or

escrow services. According to a 2008 survey of home buyers by Harris Interactive, the parent of Harris Poll, 29% of recent home buyers used a one-stop shopping service in 2008 compared to 20% in 2002 – an increase of 45%.[2]

Since real estate brokerage firms began to offer mortgage, title, and other settlement services over 20 years ago, there have been several consumer surveys and economic studies to assess their impact on the home buyer. Consumer surveys have consistently shown that consumers who use realty-based one-stop shopping programs have a more favorable home buying experience[3], and economic studies over the years have shown that they are competitive in cost.[4]

In today's challenging housing market, which has seen the failure of numerous mortgage and title firms that can threaten prompt and efficient closings, diversified real estate brokerage firms like Long and Foster are increasingly using our affiliated mortgage, title, and other settlement service companies to better enable our real customers to close on time and move into their new homes as scheduled. Because we own or partially own other companies needed to close the home purchase transaction, we are able to assure that they communicate promptly with each

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2 "One-Stop Shopping Consumer Preferences" (February 2008), performed by Harris Interactive and commissioned by the National Association of Realtors (NAR).

3 The 2008 Harris Interactive consumer survey (see footnote 1) also found that buyers who used one-stop shopping in their latest real estate transaction are more satisfied with their home buying experience (8.3) than those who used services from multiple providers (7.6). These results are consistent with a 2002 Harris Interactive survey of recent and potential home buyers that found that 82% of home buyers would "strongly" or "somewhat" strongly consider using a one stop shopping service for their home purchase, and that 64% of home buyers who recently used one stop shopping programs had a better overall experience with their home purchase transaction.

4 The most recent economic study on the costs of affiliated services vs. unaffiliated services involved an independent analysis of over 2200 HUD-1 Settlement Statements from transactions conducted in nine states (Alabama, Illinois, Maryland, Michigan, Minnesota, North Carolina, Ohio, South Carolina and Virginia) in 2003 and 2005. The study concluded that title premiums and title-related settlement closing charges are not higher when affiliated business arrangements are involved compared to when they are not. "Affiliated Business Arrangements and Their Effects on Residential Real Estate Settlement Costs" (2006), The CapAnalysis Group LLC. The CapAnalysis Study reached the same conclusion as a 1994 study performed by the national economic research firm of Lexecon, Inc., which found that title and title-related services for transactions performed by affiliated title companies in seven states – Florida, Minnesota, Tennessee, Wisconsin, Mississippi, Pennsylvania, and California – were competitive with those provided by unaffiliated title companies. "Economic Analysis of Restrictions on Diversified Real Estate Services Providers", by Lexecon, Inc., January 3, 1995.

other and we are better able to resolve any service issues that arise more efficiently than we could with independent companies.

B. The Impact of HUD's Proposed RESPA Rule on Diversified Real Estate Brokerage Companies

Diversified real estate brokerage firms are subject to RESPA's "affiliated business" provisions, which prohibit companies from "requiring the use" of an affiliated settlement service provider. HUD has long allowed companies, however, to provide voluntary discounts, rebates, and other incentives to consumers who purchase our affiliated services as long as the services are separately available and as long as the incentive is genuine, meaning it is not offset by increased prices of other services in the transaction to offset the incentive.

Because diversified real estate brokerage firms are more confident that our affiliated companies can assure a prompt and efficient closing, we commonly offer voluntary, positive incentives to customers who use our affiliated mortgage and title services under this longstanding RESPA exemption.

For example, earlier this year Long and Foster offered our real estate customers who purchase a home listed by Long and Foster and also obtain a 30-year fixed mortgage through our affiliated mortgage company, Prosperity Mortgage, a 1/2 percentage reduction in their mortgage rate over the first year – which, using an interest rate of 6%, for example, saves them $762 on a $200,000 mortgage.

Currently, we promise home buyers who use a Long and Foster listing or sales agent and also obtain a loan commitment through Prosperity Mortgage that we will pay their first month's principal and interest up to $5,000 if the loan doesn't fund.

Last year, under Long and Foster's "Helping Those Who Serve" program, we offered state and local police, firefighters, military personnel, teachers, and certified health care providers a $500 closing credit if they used Long and Foster Real Estate, Prosperity Mortgage, Long and Foster

Insurance Services, and a Prestige Settlement Agency to purchase their home. In addition, they received discounts on a variety of support services from a variety of support industries from moving companies to home supply retailers.

These programs were voluntary and if they were not used, the home buyer pays no more. But if they are used, our customers can receive substantial savings and just as importantly we were better able to assure they got to closing on time, since they are using the services of our affiliated businesses over which we have more control.

Other commonly used consumer incentives used by Long & Foster and other diversified real estate brokerage firms throughout the country include:

- Payment of all or part of the 1% mortgage origination fee
- Downpayment assistance
- A free or discounted home warranty
- A gift certificate for a Home Depot, Sears, or Lowe's purchase
- A guarantee that the provider will pay the difference if closing costs on the HUD-1 Settlement Statement exceed those on the Good Faith Estimate
- A guarantee that the title commitment will be delivered within five or ten business days from the date the title order is received
- A guarantee that the HUD-1 Settlement Statement will be delivered five days prior to settlement
- A guaranteed payment of $500 or more if closing occurs later than the date mutually agreed upon.

These voluntary consumer incentives have been well-received by real estate brokerage customers. In fact, Harris Interactive found in its 2008 home buyer survey that I referred to earlier that 77% of home buyers surveyed considered the biggest advantage of using a one-stop shopping program to be saving money through discounted prices.[5]

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[5] Other advantages that home buyers said they could obtain from one-stop shopping programs included increased efficiency and manageability (73%), convenience (73%) and things not falling through the cracks (73%).

Unfortunately, HUD proposes a new definition of "required use" in its proposed RESPA rule that would effectively prohibit companies from offering these positive, voluntary consumer incentives for the purchase of affiliated mortgage, title, or other settlement services that lower costs and enable a prompt and efficient closing.

HUD says in the Regulatory Impact Analysis that accompanies its proposed rule that it recognizes that consumers may benefit from one-stop shopping programs offered by real estate brokerage firms and homebuilders. But it says it is proposing this ban on consumer incentives because it believes that some companies are hiding discounts by increasing the price of other services – which clearly is prohibited under current RESPA regulations – or are charging more than their normal rates if the customer does not use the affiliated service – which also clearly is prohibited today.

HUD also has provided no indication that it has analyzed the types of positive, voluntary consumer incentive programs being offered throughout the industry today that provide consumers tangible savings and better service. We find it odd that HUD would overturn a 16-year-old policy that would prevent companies from offering consumers (1) lower costs in their home purchase transaction; (2) a guarantee that their closing will be on time; or (2) a guarantee that their costs at closing will not exceed those on the Good Faith Estimate without performing more research on today's marketplace activities in this area.[6]

[6] In June 11, 2008 public comments to HUD regarding its proposed RESPA rule, staff of the Federal Trade Commission (FTC) also recommended that HUD reconsider the change to the definition of "required use" in HUD's regulations:

> "FTC staff recommends that HUD reconsider the change to the definition of "required use" in HUD's regulations. The expanded definition of required use could deprive customers of the lower prices that can result from bundling related services. Bundling related services can create efficiencies in – lower the costs of – providing those services, and discounting the bundle allows consumers to pay less for the services. Indeed, HUD recognizes the potential benefits of bundling, and appropriately retains a safe-harbor to allow settlement service bundling. FTC staff believes that the analysis of settlement service bundling also applies to the analysis of other bundles. Absent clear evidence of probable harm from bundling related services, FTC staff believes that HUD should reconsider the proposed change because bundling can improve efficiency and save consumers money." Comments of the Staff of the Bureau of Consumer Protection, the Bureau of Economics, and the Office of Policy Planning of the Federal Trade Commission, June 11, 2008, page 30.

III. Summary

Mr. Chairman and Members of the Subcommittee, HUD's proposed ban on voluntary consumer incentives is another example of how HUD's proposed RESPA rule would increase costs and result in poorer service for home buyers. The rule was not well-conceived as a whole. Given the breadth of HUD's proposed RESPA rule and its potential impact on today's fragile housing market, we believe that HUD should withdraw its 2008 RESPA regulation and work with the Federal Reserve Board (Fed) which separately is revising its Truth in Lending Act (TILA) disclosures to develop uniform mortgage disclosures that would truly accomplish its goals in this rulemaking.

Thank you for the opportunity to testify, and I would be glad to answer any questions.

Testimony of

Debra Still

On Behalf of the

National Association of Home Builders

Before the

United States House of Representatives

Committee on Financial Services

Subcommittee on Oversight and Investigations

on the

U.S. Department of Housing and Urban Development's

RESPA Proposal

September 16, 2008

Introduction

Chairman Watt, Ranking Member Miller, distinguished Members of the Subcommittee on Oversight and Investigations, on behalf of the more than 235,000 members of the National Association of Home Builders (NAHB), thank you for this opportunity to testify today on the important subject of the U.S. Department of Housing and Urban Development's (HUD's) Proposed Rule to change its regulations relating to the Real Estate Settlement Procedures Act of 1974 (RESPA).

My name is Debra Still. I am president and chief executive officer of Pulte Mortgage LLC in Englewood, Colorado, which is a subsidiary of Pulte Home Corporation, a publicly traded company. I want to thank you for holding this hearing to bring focus to HUD's RESPA proposal and to explore ways this proposal can be changed to improve mortgage loan disclosures for consumers while preserving many of the benefits consumers enjoy today by being able to choose the mortgage and title alternative that best serves their needs.

In my testimony, I will broadly outline the major components of HUD's proposal. My primary focus, however, will be on HUD's proposed definition of "required use," which, if enacted as originally proposed, would have an immediate negative impact upon many consumers who purchase new homes. As proposed, this definition would prohibit a home builder from offering any incentive in exchange for a home buyer's use of the builder's affiliated mortgage or title companies or any other builder-affiliated business. In my testimony, I will describe the reasons why home builders offer these incentives to consumers and how the incentives improve the home buying experience. I will also propose an alternative definition which, if implemented, would continue to allow builder incentives while properly addressing HUD's concerns.

<u>Summary of HUD's Proposal</u>

HUD issued its proposal to revise RESPA regulations on March 14. This proposal is the latest attempt at RESPA reform by HUD. Prior to issuing this proposal, HUD had unsuccessfully proposed widespread RESPA reforms in 2002, which were withdrawn in 2004.

HUD states that its objectives in issuing the proposed revisions to RESPA are "to simplify and improve the process of obtaining home mortgages and to reduce settlement costs to consumers." A guiding principle in HUD's proposal is that increased competition among lenders, as a result of borrowers' improved ability to shop for mortgage credit, will put pressure on lenders and other settlement service providers to pass cost savings on to borrowers. To this end, HUD has proposed several changes to the Good Faith Estimate (GFE) and the HUD-1 settlement statement, including:

- A standardized four-page Good Faith Estimate (GFE) form, which is provided to a borrower prior to closing their loan, that provides a summary of loan terms and settlement charges to enable the borrower to comparison shop for a mortgage loan;

- More accurate estimates of final settlement charges through the imposition of tolerances to limit increases in GFE estimates at closing;
- Revised requirements for disclosure of mortgage brokers' commissions, or "yield spread premiums" (YSP), in detail on the GFE, including the effect various rates would have on the YSP;
- Allowing lenders and brokers to seek discounts, including volume-based discounts, for settlement services as well as the use of average cost pricing for settlement services instead of actual cost;
- Revisions to the HUD-1 loan settlement statement to facilitate comparison with the information provided on the GFE; and,
- An addendum to the revised HUD-1 that would require loan closing staff to prepare and read a specific "closing script" to borrowers that explains final loan terms and settlement costs and any differences that exist between the final terms/costs and the GFE.

In addition, HUD proposes to change the definition of "required use" to include tying an incentive to, or conditioning the ability to avoid a disincentive on, the use of a particular settlement service provider. Settlement services, or optional combination of services, from a specific settlement service provider that are less than the cost of individual settlement services would be exempted from the definition of required use.

Overview of NAHB's Position

NAHB supports HUD's stated goal of improving the mortgage process and reducing the cost of these transactions for consumers. NAHB also endorses the concept that consumers should be provided with sufficient information to enable them to understand the terms of a mortgage loan for which they are applying and that the process of shopping, or comparing loan alternatives, should be as simple and straightforward as possible.

NAHB believes that free and open competition among service providers results in the greatest benefit for consumers who are purchasing new homes. These benefits extend beyond purely financial considerations and include issues relating to certainty that home sales will close in a timely manner and that the terms, costs and characteristics of the related financing arrangements conform to the settlement services that the consumer sought.

While NAHB agrees with HUD's intent to simplify and improve the process of obtaining mortgages and to reduce hidden consumer settlement costs, we believe portions of the proposal will not meet this objective and would in fact negatively impact consumers. Of paramount concern to NAHB is the proposed change to the "required use" definition. This proposal would eliminate home builders' opportunity to offer *bona fide* incentives to consumers when the availability of those incentives is linked to consumer use of home builders' affiliated mortgage and title companies, resulting in significant increases in costs to home buyers.

The bulk of our statement will address our concerns with the proposed required use definition and the adverse impact it would have on numerous NAHB members who have affiliated mortgage and title companies, and more importantly, on consumers. As discussed further below, NAHB urges HUD to broaden the proposed definition to recognize the value that builder affiliates can bring to consumers through the loan, title and closing processes. Our statement also addresses concerns with the applicability of HUD's proposed changes to the Good Faith Estimate to the settlement process for the purchase of a newly built home.

"Required Use" Definition

RESPA regulations prohibit participants in the sale, financing and settlement of a home from requiring the buyer to use the services of an affiliated settlement service company. There is an exception for situations where the buyer is offered a service at a discounted price, or offered another incentive for using an affiliated company, as long as the use of the affiliate is optional and the discount or incentive is genuine and not made up by higher costs elsewhere in the transaction. HUD has expressed concern that the current regulatory definition of required use does not protect home buyers from confusing or disingenuous referral arrangements and, as a result, buyers are not able to determine their best option.

HUD specifically cites arrangements where a home builder offers price reductions or additional amenities on a home in exchange for the buyer's use of the builder's affiliated mortgage or title company. HUD says that consumers have complained that rates and fees charged by affiliated mortgage companies are higher than those available from unaffiliated companies; that builder incentives are imbedded in the price of the home and, therefore, are not true incentives; and, that incentives are so large that the option of not using the affiliated company results in an overwhelming penalty that compels the buyer to use the affiliate. HUD's proposed solution is to revise the required use definition in a way that excludes all persons and organizations other than settlement service providers from offering an incentive for use of an affiliated company. As a result, home builders would not be allowed to offer such incentives.

NAHB strongly disagrees with this portion of HUD's proposed revisions to the RESPA regulations. While NAHB agrees that excessive or deceptive incentives for affiliate use should not be permitted, HUD's proposal would also eliminate *bona fide* incentives, denying consumers significant savings in their home purchases. NAHB maintains that the examples of required use problems given by HUD are ambiguous and incomplete. Moreover, they do not represent the vast majority of home builders providing incentives for buyer use of affiliates, who do so in a responsible manner that brings substantial benefits to consumers.

Builders Seek Favorable Relationships with Home Buyers

Home builders have a strong interest in establishing and maintaining positive relationships with their buyers. When developing communities, builders are not involved

in short-term, one-time transactions. Home builders commit millions of dollars in resources and significant human capital toward the planning and construction of the communities they develop. Most builders construct and sell homes in the same communities year after year and, therefore, place a premium on maintaining a reputation built through favorable customer reviews and exemplary corporate citizenship.

Builders look to purchasers of their homes for repeat business and referrals, which is not possible unless consumers are satisfied with their home purchases and related settlement service transactions. Consumers will only refer their friends and relatives to a builder when they believe they have been treated fairly and received excellent value for their investment. A good reputation in the home building business takes many years and transactions to establish, but this hard-earned reputation could be easily tarnished by a handful of bad experiences. The last thing home builders want is to have disgruntled purchasers.

In addition, an integral component of that effort is ensuring that consumers receive competitively priced mortgages that enable them to enjoy their homes without undue financial burden. Therefore, it is in a home builder's self interest to make every effort to avoid foreclosures, which harm consumers and the communities in which they live.

In order to ensure that high customer satisfaction levels are achieved and maintained through the home buying and mortgage financing processes, many home builders conduct post-purchase customer satisfaction surveys at closing and at regular intervals afterward. J.D. Power and Associates also conducts surveys in certain markets, as cited in HUD's Regulatory Impact Analysis, which states,

> "A recent study by J.D. Power found that the majority of borrowers surveyed who finance through a builder's affiliate were satisfied with the experience. According to J.D. Power, borrowers claimed that they chose to borrow from builder affiliates because the interest rates were competitive and that the process was easier."[1]

The home building business is highly competitive, with over 80,000 firms engaged in the primary business of building and selling single family residences. If a home builder does not offer consumers new homes at fair prices, combined with settlement services at fair terms, these consumers will choose a more desirable alternative.

The process of buying a new home, with the myriad of choices and options, is very complex and often requires several months to consummate. Understandably, home builders want these complex transactions to flow as smoothly as possible and they strive to ensure that consumers' home buying experiences are as positive as possible.

Why do home builders establish affiliates?

As part of the effort to build strong consumer relationships, many home builders have established settlement service affiliates, such as mortgage and title companies. A

[1] RESPA Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis, page 3-79.

number of NAHB's builder members have established wholly-owned mortgage and title affiliates or have formed joint ventures with mortgage lenders and title companies. Collectively, these relationships have successfully facilitated home purchases for hundreds of thousands, perhaps millions, of consumers over a span of more than a decade.

Home building companies that have affiliated mortgage and title companies have formed these affiliates primarily to improve the overall customer experience and to improve the likelihood that the home sale closing occurs as promised and in a timely manner. For home builders, these affiliates provide economic benefits to the consumer that far outweigh the income received from the builders' ownership in the businesses.

In the conditions that have prevailed during the past year, where mortgage financing has become unstable and uncertain, these relationships have taken on greater importance. Many home builders can document sales numbering in the hundreds that were originally scheduled to have been financed by outside lenders that failed to take place and were subsequently "saved" by the builder's affiliated mortgage company. Had the builder's affiliate not been prepared to step in at the eleventh hour, it is unlikely that these consumers would have been able to move forward with their purchase. If they did, their mortgage would have had much less favorable terms.

An explanation of the complexity of the home building business might help to put into perspective a few of the reasons builders establish mortgage and title affiliates. At any given time, some builders may have much of their backlog of homes under construction. The affiliate relationship fosters a high degree of accountability between the builders and affiliates, which leads to well-coordinated, efficient transactions that have a high likelihood of closing on time without any "surprises" for the consumer or builder.

In the home building business, there is typically a push by consumers, sellers and lenders to close the bulk of home purchases at the end of each month. Without the coordination, communication and focus afforded by home builders' affiliates, opportunities increase for slip-ups that delay closings. Every loan that fails to close on time represents a tremendous inconvenience for a new home buyer and also carries significant additional inventory, marketing and reputational costs for a home builder.

Studies of builder-affiliated mortgage companies conducted by the research firm Wholesale Access have found that builder-affiliated mortgage companies have lower per-loan operating costs as compared to outside lenders[2]. The savings from these economies and the other affiliate benefits are difficult to quantify; however, they are significant and are routinely passed along to consumers in the form of incentives for use of a builder affiliate.

In practice, these affiliated relationships allow builders to manage their primary business of building and selling homes with far greater economic efficiency. HUD's

[2] Builder Benchmark – A Production Revenue and Expense Comparison, a series of private surveys conducted for selected builder-affiliated mortgage companies by Wholesale Access Mortgage Research and Consulting, 2001-2006.

proposal fails to account for the substantial savings that builders realize through affiliated businesses, and are able to pass on to consumers. Contrary to HUD's assertion, home builders in general do not increase the selling prices of homes to offset these incentives. The competitiveness of the marketplace simply doesn't allow this to occur.

Builder Affiliates Compete for Business

It is important to note that the sales personnel of home builders are free to refer consumers to any mortgage and title company and place top priority on ensuring that the home sale will close smoothly and on time. Therefore, builder-affiliated mortgage companies must compete for every referral. Service and price are the primary factors that determine if a home builder's sales representative refers a home buyer to a particular lender. Surveys conducted from 2001 through 2006 indicate that builder-affiliated mortgage companies can expect to finance sixty to eighty percent of the sales of their related builders[3]. That these capture rates have remained relatively steady over several years is a strong testament to the competitive nature of the settlement services marketplace as well as to consistent quality of service the affiliated mortgage and title companies provide to purchasers of the parent companies' homes.

Proposed HUD Definition

NAHB does not believe HUD has established a sound basis for the proposed changes in the definition of required use. HUD supports its proposal entirely with anecdotal, incomplete and unsubstantiated examples that have been advanced previously by outspoken opponents of affiliated businesses.[4] The examples cited as problems appear to be violations under the current RESPA regulations and could be addressed accordingly.

Furthermore, HUD has not provided any empirical studies or other statistical information that substantiate its position that consumers are harmed by using builder affiliated service providers. NAHB suggests that, in developing this proposal regarding required use, HUD's research does not conform to the data quality requirements that are imposed upon all federal rulemakings by the statute commonly known as the Information Quality Act.[5]

HUD's final Information Quality Guidelines as published in the Federal Register on November 18, 2002, read as follows: "HUD will ensure that the information it disseminates to the public is objective (accurate, clear, complete and unbiased), useful, and has integrity." NAHB submits that the justification for the proposed changes to the required use definition does not meet these criteria.

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[3] Ibid.

[4] RESPA Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis, pages 3-77 and 3-78.

[5] Section 515 of the Treasury and General Government Appropriations Act for Fiscal Year 2001, Public Law 106–554.

NAHB Recommendation

As previously stated, NAHB believes HUD has not provided adequate justification to change the required use definition. However, if HUD proceeds with changes to the definition, NAHB suggests the following:

> "**Required use** means a situation in which a person's access to some distinct service, property, discount, rebate or other economic incentive, or the person's ability to avoid an economic disincentive or penalty, is contingent upon the person using or failing to use one or more referred providers of settlement services, and the person will pay more than fifty percent (50%) of the total charges of the applicable settlement service provider(s), either directly or by payment of a charge, all or part of which is used to pay for the settlement service(s). An offer of any benefit to the person by any individual or entity based on the person's use of one or more particular settlement service providers does not constitute a required use of the provider(s) if the following conditions are satisfied:
>
> 1. The offered benefit consists of one or both of the following, or any combination thereof:
>
>   a. The payment, or provision of funds or a credit for the payment, of one or more financing, closing and/or settlement costs of any provider(s) in any amount, or a reduction of one or more of such costs by any amount.
>
>   b. The payment, or provision of funds or a credit for the payment, of the base price of a home, the price of any option(s) for the home and/or the price of any upgrade(s) for the home, or a reduction of the base price of the home, of the price of any option(s) and/or the price of any upgrade(s), in a total amount up to six percent (6%) of the pre-discounted base price of the home.
>
> 2. The person has a choice to accept or decline the benefit arrangement.
>
> 3. The total amount payable by the person for the financing, closing and settlement costs and the property being purchased, with any options and upgrades, in connection with the transaction would be higher without the offered benefit.
>
> Additionally, the purchase by a builder or seller from a lender of a forward commitment pursuant to which the lender will make an aggregate amount of financing available to purchasers of homes from the builder or seller under the terms of the commitment does not constitute a required use of the lender. The terms of the commitment may include, without limitation, financing at a combination of interest rate and points that is lower than otherwise available from the applicable lender without the commitment. Without limiting the foregoing, there is no required use of a lender if a home purchaser obtains financing from a lender pursuant to such a forward commitment, and also accepts an offered benefit

satisfying the conditions set forth above that is based on the use of the same or a different lender."

In explanation of the alternative proposal:

- The NAHB proposal uses the term "person" to refer to the party who is offered a benefit, rather than "borrower." HUD's proposal uses the term "borrower," which appears to be too narrow to encompass all types of purchasers of settlement services.

- The NAHB proposal refers to the party that can offer a benefit as an individual or entity. This is because the definition of "person" under RESPA refers to individuals, corporations, associations, partnerships and trusts, but not limited liability companies.

- Following HUD's approach, the NAHB proposal includes access to a discount, rebate or other economic incentive that is tied to use of a particular provider as a required use. The result is that benefits tied to the use of an affiliate or a particular title company would be limited to settlement/closing cost discounts and the like and/or home, option and upgrade discounts and the like. The home-related incentives would be limited to a specific percentage of the home sales price. This is consistent with HUD's goal to better define what benefits qualify as exceptions to the general required use prohibition.

- The proposal includes the element from the existing definition that a person must pay for a service in order to have a required use, but establishes a floor that would require the person to pay more than 50% of the applicable charge(s). If a person paid 50% or less of the charges of the applicable provider, there would be no required use of the provider. Instead of using the current language that the person pays for the service directly or pays a charge "attributable, in whole or in part, to the settlement service," the NAHB proposal would require that the person pay more than 50% of the total charges of the applicable settlement service provider directly or by payment of charge, "all or part of which is used to pay for the settlement service(s)."

- The definition seeks to better define the condition that the benefit arrangement be optional to the person by stating as a condition that the person has a choice to accept or decline the benefit arrangement. The intent is to avoid the concept of "optional" that could still present issues as to the interpretation of what is "optional." As drafted, the alternate proposal avoids this complication by requiring simply that the person has a choice to accept or decline the benefit.

- A third condition addresses HUD's concern as to whether a benefit provides a "true discount." The approach is that the total costs to the person of the transaction (home and settlement/closing costs) with the benefit is lower than the total costs

without the benefit. Simply stated, if the deal with the benefit is at a lower cost, then the benefit must provide a "true discount."

- The NAHB proposal includes the clarification that forward commitment arrangements for financing do not constitute a required use, even if combined with a benefit arrangement that involves the same or a different lender. Under the proposal, the "terms of the commitment" may, but do not have to, provide for a lower combination of rates and points than is otherwise available. The Fannie Mae forward commitment exception does not require lower rates. In various cases, such as the market today, simply having a guaranteed source of financing for home purchasers is a benefit to the purchasers. Of course, the "terms of the commitment" could include better rate and point combinations.

Good Faith Estimate

In NAHB's comment letter to HUD on the 2002 RESPA proposal, we raised our concerns relating to the special circumstances involved in processing mortgages for newly built homes: "Originating mortgages for the purchase of newly constructed homes; which typically commences at the start of a construction period of four to nine months or longer, requires special attention."[6]

NAHB's 2002 comment letter describes the ways in which HUD's earlier proposal failed to recognize or accommodate situations where the price of a newly built home may change many times while the home buyer goes through the process of selecting options for the home. A home buyer's credit situation also may change for the better or worse during the construction period, which could change the purchaser's mortgage financing options, including, but not limited to, the rate and terms of loans for which a purchaser may qualify. In the current proposal, it appears that HUD has once again failed to recognize these factors which are unique to new construction.

HUD's proposal seeks to restrict changes in the GFE that occur within sixty days of the loan closing only to those changes that have occurred as a result of "unforeseeable circumstances." Clearly, numerous changes in the price of a new home that result from selections of options can and do occur, sometimes until a few days before the sale is closed. Such changes are material and are not unforeseen; however, these changes would require the lender to issue a new GFE. In addition, a change in the sale price of a home may change other related costs, such as recordation- and title-associated fees and expenses, and might even require changes in the terms of the buyer's loan.

The general rules HUD has proposed regarding the GFE do not mandate a minimum period of time that a GFE must be issued before settlement dates. Thus, mandating a sixty-day period under the new home exception is not warranted.

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[6] National Association of Home Builders comment letter, Docket No. FR-4727-P-01, October 28, 2002, page 2.

Furthermore, in a new construction home purchase scenario, it may not be possible to ascertain with precision the closing date for the sale. For example, if a lender issued a revised GFE sixty days in advance of an anticipated closing, and the home was completed several days ahead of schedule, therefore allowing the loan to be closed earlier than originally anticipated, the GFE would no longer be in compliance with HUD's proposed GFE requirements.

NAHB recommends that HUD either reduce the GFE sixty-day window to a more reasonable timeframe (and in no event greater than 14 days) or offer a broader exception for situations that involve the purchase of a newly built home to account for the greater potential for variations in such transaction than in transactions involving the sales of existing homes. NAHB also recommends that if a minimum period is established, that the period be based on the anticipated settlement date at the time the GFE is issued, and not the actual settlement date.

Conclusion

In conclusion, NAHB supports efforts to make the process of shopping for and obtaining a mortgage more transparent, straightforward and less expensive for consumers. However, NAHB disagrees with several aspects of the regulatory changes HUD has proposed to accomplish these goals.

We do not believe that HUD's analysis supports the conclusion that home builders should be prohibited from offering consumers the option to realize cost savings and other benefits that accrue through consumers' use of builders' affiliated mortgage and title companies. In its comments to HUD, NAHB has offered an alternative to the proposed definition of required use, which if adopted, would permit home builders to continue to offer *bona fide* and reasonable incentives in exchange for consumers' use of affiliated companies. Prohibiting such incentives would result in significant increases in home purchase costs and undermine critical financing support at a time of severe mortgage and housing market turbulence.

NAHB also is concerned that the proposed timing and restrictions regarding the Good Faith Estimate do not account for situations involving newly built homes and urges HUD to reconsider its proposal in this regard.

In closing, Mr. Chairman, I want to reiterate NAHB's opposition to HUD's proposed definition of "required use." I would welcome any questions you may have.

Friday,
March 14, 2008

Part III

Department of Housing and Urban Development

24 CFR Parts 203 and 3500

Real Estate Settlement Procedures Act (RESPA): Proposed Rule To Simplify and Improve the Process of Obtaining Mortgages and Reduce Consumer Settlement Costs; Proposed Rule

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

24 CFR Parts 203 and 3500

[Docket No. FR–5180–P–01]

RIN 2502–AI61

Real Estate Settlement Procedures Act (RESPA): Proposed Rule To Simplify and Improve the Process of Obtaining Mortgages and Reduce Consumer Settlement Costs

AGENCY: Office of the Assistant Secretary for Housing—Federal Housing Commissioner, HUD.

ACTION: Proposed rule.

SUMMARY: This proposed rule presents HUD's proposal to simplify and improve the disclosure requirements for mortgage settlement costs under the Real Estate Settlement Procedures Act of 1974 (RESPA), to protect consumers from unnecessarily high settlement costs. This proposed rule takes into consideration: discussions during HUD's RESPA Reform Roundtables held in July and August 2005; public comments in response to HUD's July 29, 2002, proposed rule that addressed RESPA reform; and comments received and views expressed through congressional hearings; meetings with affected parties; and consultation with other federal agencies, including the Small Business Administration Office of Advocacy.

HUD's objective in proposing these revisions is to protect consumers from unnecessarily high settlement costs by taking steps to: Improve and standardize the Good Faith Estimate (GFE) form, to make it easier to use for shopping among settlement service providers; ensure that page one of the GFE provides a clear summary of the loan terms and total settlement charges so that borrowers will be able to use the GFE to comparison shop among loan originators for a mortgage loan; provide more accurate estimates of costs of settlement services shown on the GFE; improve disclosure of yield spread premiums to help borrowers understand how they can affect their settlement charges; facilitate comparison of the GFE and the HUD–1/HUD–1A Settlement Statements (HUD–1 settlement statement or HUD–1); ensure that at settlement borrowers are made aware of final loan terms and settlement costs, by reading and providing a copy of a "closing script" to borrowers; clarify HUD–1 instructions; clarify HUD's current regulations concerning discounts; and expressly state when RESPA permits certain pricing mechanisms that benefit consumers, including average cost pricing and discounts, including volume based discounts.

DATES: *Comment Due Date:* May 13, 2008.

ADDRESSES: Interested persons are invited to submit comments regarding this proposed rule. There are two methods for comments to be submitted as public comments and to be included in the public comment docket for this rule. Regardless of the method selected, all submissions must refer to the above docket number and title.

1. *Submission of Comments by Mail.* Comments may be submitted by mail to the Regulations Division, Office of General Counsel, Department of Housing and Urban Development, 451 Seventh Street, SW., Room 10276, Washington, DC 20410–0001.

2. *Electronic Submission of Comments.* Interested persons may submit comments electronically through the Federal eRulemaking Portal at *www.regulations.gov*. HUD strongly encourages commenters to submit comments electronically. Electronic submission of comments allows commenters maximum time to prepare and submit comments, ensures timely receipt by HUD, and enables HUD to make them immediately available to the public. Comments submitted electronically through the *www.regulations.gov* Web site can be viewed by other commenters and interested members of the public. Commenters should follow the instructions provided on that site to submit comments electronically.

Note: To receive consideration as public comments, comments must be submitted through one of the two methods specified above. Again, all submissions must refer to the docket number and title of the rule. No Facsimile Comments. Facsimile (FAX) comments are not acceptable.

Public Inspection of Public Comments. All properly submitted comments and communications submitted to HUD will be available, without charge, for public inspection and copying between 8 a.m. and 5 p.m. weekdays at the above address. Due to security measures at the HUD Headquarters building, an advance appointment to review the public comments must be scheduled by calling the Regulations Division at (202) 708–3055 (this is not a toll-free number). Individuals with speech or hearing impairments may access this number through TTY by calling the toll-free Federal Information Relay Service at (800) 877–8339. Copies of all comments submitted are available for inspection and downloading at *www.regulations.gov*.

FOR FURTHER INFORMATION CONTACT: Ivy Jackson, Director, or Barton Shapiro, Deputy Director, Office of RESPA and Interstate Land Sales, U.S. Department of Housing and Urban Development, 451 Seventh Street, SW., Room 9158, Washington, DC 20410; telephone number (202) 708–0502 (this is not a toll-free number). For legal questions, contact Paul S. Ceja, Assistant General Counsel for GSE/RESPA, Joan L. Kayagil, Deputy Assistant General Counsel for GSE/RESPA or Rhonda L. Daniels, Attorney-Advisor for GSE/RESPA, Room 9262; telephone number (202) 708–3137. Persons with hearing or speech impairments may access this number via TTY by calling the toll-free Federal Information Relay Service at (800) 877–8339. The address for the above listed persons is: Department of Housing and Urban Development, 451 Seventh Street, SW., Washington, DC 20410.

SUPPLEMENTARY INFORMATION:

I. Introduction and Principles

The process for disclosing settlement costs in the financing or refinancing of a home is regulated under RESPA, 12 U.S.C. 2601–2617. HUD seeks to make improvements to its regulations implementing RESPA (24 CFR part 3500), to make the process clearer and more useful and ultimately less costly for consumers. The mortgage industry has changed considerably since RESPA was enacted in 1974, and the regulations implementing RESPA's original disclosure requirements are no longer adequate.

The settlement costs associated with a mortgage loan are significant. In the case of purchase transactions, these costs can become an impediment to homeownership, particularly for low- and moderate-income households. HUD's current RESPA rules do not facilitate shopping or competition to lower these costs. HUD estimates that with the changes proposed to its RESPA regulations in this rulemaking, settlement costs will be lowered by $6.5 to $8.4 billion annually, with an average savings of $518 to $670 per transaction.

RESPA's purposes include the provision of effective advance disclosure of settlement costs and elimination of practices that tend to unnecessarily increase the costs of settlement services. Similarly, the Administration is committed to extending homeownership opportunities. HUD's regulatory reform and enforcement efforts for RESPA

remain guided by the following principles:

1. Borrowers should receive loan terms and settlement cost information early enough in the process to allow them to shop for the mortgage product and settlement services that best meet their needs;

2. Costs should be disclosed and should be as firm as possible to avoid surprise charges at settlement;

3. Many of the current problems arise from the complexity of the mortgage loan settlement process. The process can be improved with simplification of disclosures and better borrower information;

4. Increased shopping by borrowers will lead to greater pricing competition, so that market forces will lower prices and lessen the need for regulatory enforcement;

5. The key final terms of the loan a borrower receives should be disclosed to the borrower in an understandable way at closing; and

6. HUD will continue to vigorously enforce RESPA to protect borrowers and ensure that honest settlement service providers can compete for business on a level playing field.

II. RESPA Overview

Congress enacted the Real Estate Settlement Procedures Act of 1974 (Pub. L. 93–533, 88 Stat. 1724, 12 U.S.C. 2601–2617) after finding that "significant reforms in the real estate settlement process are needed to ensure that consumers throughout the Nation are provided with greater and more timely information on the nature and costs of the settlement process and are protected from unnecessarily high settlement charges caused by certain abusive practices * * *." (12 U.S.C. 2601(a)). RESPA's stated purpose is to "effect certain changes in the settlement process for residential real estate that will result:

"(1) In more effective advance disclosure to home buyers and sellers of settlement costs;

"(2) In the elimination of kickbacks or referral fees that tend to increase unnecessarily the costs of certain settlement services;

"(3) In a reduction in the amounts home buyers are required to place in escrow accounts established to insure the payment of real estate taxes and insurance; and

"(4) In significant reform and modernization of local recordkeeping of land title information." (12 U.S.C. 2601(b)).

RESPA's requirements apply to transactions involving "settlement services" for "federally related mortgage loans." Under the statute, the term "settlement services" includes any service provided in connection with a real estate settlement.[1] The term "federally related mortgage loan" is broadly defined to encompass virtually all purchase money and refinance mortgages.[2]

Section 4(a) of RESPA (12 U.S.C. 2603(a)) requires the Secretary to develop and prescribe "a standard form for the statement of settlement costs which shall be used * * * as the standard real estate settlement form in all transactions in the United States which involve federally related mortgage loans." The law further requires that the form "conspicuously and clearly itemize all charges imposed upon the borrower and all charges imposed upon the seller in connection with the settlement * * *" (Id).

Section 5 of RESPA (12 U.S.C. 2604) requires the Secretary to prescribe a Special Information Booklet for borrowers. Sections 5(c) and (d) of RESPA require each lender to provide a Good Faith Estimate (GFE), as prescribed by the Secretary, within 3 days of loan application, and that the GFE state "the amount or range of charges for specific settlement services the borrower is likely to incur in connection with the settlement * * *."

In 1990, language was added in Section 6 of RESPA (12 U.S.C. 2605) to require certain disclosures to each borrower, both at the time of loan application and during the life of the loan, about the servicing of the loan.

Section 8(a) of RESPA (12 U.S.C. 2607(a)) prohibits persons from giving and from accepting "any fee, kickback, or thing of value pursuant to any agreement or understanding, oral or otherwise, that [real estate settlement service business] shall be referred to any person" (12 U.S.C. 2607(a)). Section 8(b) of RESPA prohibits persons from giving and from accepting "any portion, split, or percentage of any charge made or received for the rendering of a real estate settlement service * * * other than for services actually performed" (12 U.S.C. 2607(b)). Section 8(c) provides, in part, that "[n]othing in [Section 8] shall be construed as prohibiting * * * (2) the payment to any person of a *bona fide* salary or compensation or other payment for goods or facilities actually furnished or for services actually performed, * * * or (5) such other payments or classes of payments or other transfers as are specified in regulations prescribed by the Secretary, after consultation with the Attorney General, the Administrator of Veterans' Affairs, the Federal Home Loan Bank Board,[3] the Federal Deposit Insurance Corporation, the Board of Governors of the Federal Reserve System, and the Secretary of Agriculture" (12 U.S.C. 2607(c)(2)).

Section 9 of RESPA (12 U.S.C. 2608) forbids any seller of property from requiring, directly or indirectly, buyers to purchase title insurance covering the property from any particular title company. Section 10 of RESPA (12 U.S.C. 2609) limits the amounts that lenders or servicers may require borrowers to deposit in escrow accounts, and requires servicers to provide borrowers with both initial and annual escrow account statements. Section 12 of RESPA (12 U.S.C. 2610) prohibits lenders and loan servicers from imposing any fee or charge on any other person for the preparation and submission of the uniform settlement statement required under Section 4 of RESPA or the escrow account statements required under Section 10(c) of RESPA, or for any statements required by the Truth in Lending Act (TILA).

Section 18 of RESPA (12 U.S.C. 2616) provides that the Act does not annul, alter, affect, or exempt any person from complying with the laws of any State with respect to settlement practices,

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[1] "Settlement services" include "* * * title searches, title examinations, the provision of title certificates, title insurance, services rendered by an attorney, the preparation of documents, property surveys, the rendering of credit reports or appraisals, pest and fungus inspections, services rendered by a real estate agent or broker, the origination of a federally related mortgage loan (including, but not limited to, the taking of loan applications, loan processing, and the underwriting and funding of loans), and the handling of the processing, and closing of settlement." 12 U.S.C. 2602(3). The term is further defined at 24 CFR 3500.2.

[2] The term "federally related mortgage loan" generally includes a loan that both: (i) Is "secured by a first or subordinate lien on residential real property (including individual units of condominiums and cooperatives) designed principally for the occupancy of from one to four families"; and (ii) is "made in whole or in part by any lender the deposits or accounts of which are insured by any agency of the Federal Government, or is made in whole or in part by any lender which is regulated by any agency of the Federal Government"; or "is made * * * or insured, guaranteed, supplemented, or assisted in any way, by [HUD] or any other officer or agency of the Federal Government or * * * in connection with a housing or urban development program administered by [HUD]" or other federal officer or agency; or "is intended to be sold * * * to [Fannie Mae, Ginnie Mae, Freddie Mac], or a financial institution from which it is to be purchased by [Freddie Mac]; or is made in whole or in part by any creditor * * * who makes or invests in residential real estate loans aggregating more than $1,000,000 per year * * *." 12 U.S.C. 2602(1).

[3] The Federal Home Loan Bank Board (FHLBB) was abolished effective October 8, 1989, by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) (Pub. L. 101–73, 103 Stat. 183). Its successor agency, the Office of Thrift Supervision, Department of the Treasury, assumed the FHLBB's regulatory functions. 12 U.S.C. 1462a(e).

"except to the extent that those laws are inconsistent with any provision of [RESPA], and then only to the extent of the inconsistency." Section 18 further authorizes the Secretary to determine whether such inconsistencies exist, but provides that the Secretary may not determine a State law to be inconsistent with RESPA if the Secretary determines the State law gives greater protection to consumers.

Section 19 of RESPA (12 U.S.C. 2617), among other provisions, authorizes the Secretary to seek to achieve the purposes of RESPA by prescribing regulations, making interpretations, and granting reasonable exemptions for classes of transactions.

III. Overview of HUD's Efforts Since 2002

On July 29, 2002 (67 FR 49134), HUD issued a proposed RESPA reform rule "Real Estate Settlement Procedures Act (RESPA); Simplifying and Improving the Process of Obtaining Mortgages to Reduce Settlement Costs to Consumers" (2002 Proposed Rule) that would have provided for a revised GFE that would have simplified and standardized estimated settlement cost disclosures to make such estimates more reliable, as well as to prevent unexpected charges at settlement. In addition, the 2002 Proposed Rule would have modified mortgage broker compensation disclosure requirements and would have provided an exemption from Section 8 of RESPA for guaranteed packages of settlement services.

The 2002 Proposed Rule followed several years of consultation with industry, consumer, and government groups on changes to RESPA. The 2002 Proposed Rule also followed two reports to Congress that examined ideas to improve the mortgage loan settlement process: The 1998 joint report by HUD and the Board of Governors of the Federal Reserve (Federal Reserve or the Board) on reform of RESPA and the Truth in Lending Act; and the 2000 HUD-Treasury Report on Predatory Lending. Both of these reports are described in more detail in the 2002 Proposed Rule (see 67 FR at 49143–6).

In response to the 2002 Proposed Rule, HUD received over 40,000 comments, of which 400 contained in-depth discussions of various issues raised by the proposal. Comments were submitted by real estate, mortgage broker, banking, mortgage lending, financial services, and title industry trade groups; consumer advocacy organizations; mortgage companies; settlement service providers; banks; credit unions and related organizations; State agencies; Members of Congress; lawyers; and other concerned persons.

Generally, the extensive comment letters supported the overall goals of the proposal, but disagreed with or expressed reservations concerning specific aspects of the proposal. For example, some lender organizations (including the Mortgage Bankers Association) strongly supported the packaging proposal, while the National Association of Realtors supported the GFE changes. Consumer advocacy organizations (including AARP and the National Consumer Law Center) largely supported the mortgage broker compensation disclosure changes, the other GFE changes; and, subject to some exceptions, the packaging proposal. Several industry organizations supported better disclosure of total mortgage broker compensation. On the other hand, the National Association of Mortgage Brokers opposed HUD's proposed approach to disclosing the yield spread premium as part of the total mortgage broker compensation, and the American Land Title Association opposed HUD's packaging proposal and offered a two-package approach as an alternative.

In response to the considerable and varied comments from the public, as well as from other federal agencies and Congress, the Secretary withdrew the proposed rule in early 2004. At that time, the Secretary committed HUD to gather additional information about settlement service costs and the process of obtaining mortgages, as well as to engage in outreach to Congress, members of potentially affected industries, consumers, and other federal agencies, before proceeding with any proposed changes related to HUD's RESPA regulations.

In June 2004, in preparation for outreach to the industry and consumer groups, HUD began consulting with its federal agency partners, including the Small Business Administration (SBA) Office of Advocacy, on RESPA reform. These meetings continued through 2005. In Spring 2005, HUD also consulted with Members of Congress and congressional staff on RESPA reform.

After these initial consultations, in July and August 2005, HUD held a series of seven consumer and industry roundtables both at HUD Headquarters in Washington, DC, and jointly with the SBA Office of Advocacy in Chicago, Los Angeles, and Fort Worth. As discussed in the public notice announcing the roundtables (70 FR 37646, June 29, 2005), in selecting participants for the roundtables, HUD sought a cross-section of representatives of consumer advocacy organizations, all segments of the settlement services industry, State mortgage industry regulators, and other interested persons who had analyzed the 2002 Proposed Rule or had offered alternative proposals for HUD's consideration. Over 150 companies, organizations, and other persons were invited to attend, and 122 of these attended at least one of the roundtables.

At the roundtables, HUD presented an overview of an approach to RESPA reform that included revision of the GFE, clarification of the yield spread premium disclosure, and the option of providing an exemption from the Section 8 provisions prohibiting referral fees, kickbacks, and unearned fees to encourage packaging of settlement services. After HUD's presentation, participants were encouraged to present their views on RESPA reform issues.

Participants generally agreed that HUD should pursue revision of the GFE. Many participants stated that the GFE should reflect the HUD–1 settlement statement, so that borrowers could better compare the GFE to the HUD–1. Consumer representatives stated that disclosure of the yield spread premium (YSP) is necessary, while mortgage brokers recommended that the YSP disclosure be dropped from the GFE. Mortgage broker participants noted that lenders are not required to disclose any secondary market fees on otherwise identical loans. Mortgage brokers expressed concern that focusing on a requirement for more effective disclosure of YSPs puts mortgage brokers at a severe disadvantage, as compared to lenders, in originating a loan. Lenders maintained that it would be impractical for a lender to disclose on the GFE how much a lender would earn if or when the loan is sold on the secondary market. These concepts also are discussed in more detail in HUD's Real Estate Settlement Procedures Act Statement of Policy 2001–1 (66 FR 53052, at 53256–7, October 18, 2001).

With respect to packaging, small business representatives asserted that a Section 8 exemption for packaging would be harmful to small business providers of settlement services because lenders would dominate packaging and would extract kickbacks from small businesses in exchange for inclusion in a package. Consumer groups opposed packaging with a Section 8 exemption on the grounds that the exemption would provide a safe harbor for loans with high costs and fees and other potentially predatory features. These groups also asserted that there would be no way to determine costs and fees for packaged loans for purposes of determining compliance with the Truth

in Lending Act. Lender representatives generally supported packaging under a Section 8 exemption as the most efficient method to ensure cost savings to consumers, but some indicated that packaging could also be delivered with limited Section 8 relief, such as for volume-based discounts and average cost pricing.

IV. This Proposed Rule

A. Generally

Today's proposed rule builds on all of this history and specifically recognizes many of the suggestions made at the roundtables with respect to the GFE and comparability of the HUD–1. The rule proposes a new framework under RESPA that would:

(1) Improve and standardize the GFE form to make it easier to use for shopping among settlement service providers;

(2) Ensure that page one of the GFE provides a clear summary of loan terms and total settlement charges so that borrowers will be able to use the GFE to comparison shop among loan originators for a mortgage loan;

(3) Provide more accurate estimates of costs of settlement services shown on the GFE;

(4) Improve the disclosure of yield spread premiums to help borrowers understand how they can affect their settlement charges;

(5) Facilitate comparison of the GFE and the HUD–1/HUD–1A Settlement Statements (HUD–1 settlement statement or HUD–1);

(6) Ensure that at settlement, borrowers are aware of final loan terms and settlement costs, by reading and providing a copy of a "closing script" to borrowers;

(7) Clarify HUD–1 instructions;

(8) Clarify HUD's current regulations concerning discounts; and

(9) Expressly state when RESPA permits certain pricing mechanisms that benefit consumers, including average cost pricing and discounts, including volume-based discounts.

A detailed description of each aspect of the proposed rule that involves these concepts follows in Sections B–E of this preamble.

This proposal also includes certain technical amendments to the current RESPA rules, as set forth below.

B. Legislative Proposals Related to RESPA Reform

In order to further bolster consumer protection, as well as to ensure uniform and consistent enforcement under RESPA, HUD intends to seek legislative changes to RESPA that will complement the regulatory improvements made in this rule. HUD firmly believes that the proposed rule will improve the mortgage loan settlement process through better disclosures to consumers, but greater consumer protection can be achieved by also strengthening certain statutory disclosure requirements and improving the remedies available under RESPA.

In today's proposed rule, HUD seeks to ensure that consumers are provided with meaningful and timely information. While HUD can make certain regulatory improvements to the disclosures that will help consumers shop for mortgage loans, HUD needs additional statutory authority to make further warranted improvements in disclosures that will help consumers understand the final terms of the loans and costs to which they commit at closing. Moreover, as currently framed, RESPA establishes limited and inconsistent enforcement authority, and does not provide HUD with any enforcement authority for key disclosure provisions. The 1998 joint report by HUD and the Federal Reserve on reform of RESPA and the Truth in Lending Act recommended that RESPA be amended to provide for more effective enforcement.[4] In its April 2007 report on the title insurance industry, the Government Accountability Office recommended that Congress consider whether modifications to RESPA are needed to better achieve its purposes, including by providing HUD with increased enforcement authority.[5]

As part of its efforts to improve the protections provided under RESPA, HUD intends to seek statutory modifications that would include the following provisions: (1) Authority for the Secretary to impose civil money penalties for violations of specific RESPA sections, including sections 4 (provision of uniform settlement statement), 5 (GFE and special information (settlement costs) booklet), 6 (servicing), 8 (prohibition against kickbacks, referral fees, and unearned fees), 9 (title insurance), and portions of 10 (escrow accounts), as well as authority for the Secretary and State regulators to seek injunctive and equitable relief for violations of RESPA; (2) requiring delivery of the HUD–1 to the borrower 3 days prior to closing; and (3) a uniform and expanded statute of limitations applicable to governmental and private actions under RESPA.

[4] See Section III of this preamble.

[5] *Title Insurance: Actions Needed to Improve Oversight of the Title Industry and Better Protect Consumers*, Government Accountability Office, April 2007, GAO–07–401.

RESPA does not currently provide HUD with enforcement mechanisms for some of the most important consumer disclosures, including the section 4 requirements related to provision of the HUD–1, and section 5 requirements related to provision of the GFE and the special information (settlement costs) booklet. HUD believes that a lack of enforcement authority and of clear remedies for violations of critical sections of RESPA negatively impacts consumers and diminishes the effectiveness of the statute. Accordingly, HUD intends to seek authority to impose civil money penalties to enforce violations of RESPA. In addition to civil money penalty authority, HUD intends to seek authority for additional injunctive and equitable remedies for violations of RESPA.

Improving the ability of consumers to shop for the best mortgage loan and control settlement costs—using the new GFE form and comparing it to the HUD–1 at closing—is a key component of today's proposed rule. Additional statutory authority would enable HUD to improve its efforts at providing borrowers with necessary and timely information about their mortgage loans and other settlement services. Section 4 of RESPA currently provides that a borrower may request to inspect the HUD–1 the day before settlement, but many borrowers are unaware of this right, and the time currently provided to inspect the HUD–1 allows little margin for identifying and challenging problematic charges before settlement.

HUD also intends to seek reform of the statute of limitations provisions of RESPA. Currently, there are different limitation periods depending on which section of the statute is alleged to have been violated, and who is pursuing a remedy of the violation. HUD believes that enforcement efforts would be enhanced, and the requirements of the statute simplified, by standardizing the statute of limitations.

C. Federal Reserve Board Proposed Rule Amending Regulation Z

On January 9, 2008, the Federal Reserve Board (Board) issued a proposed rule that would amend its Regulation Z which implements the Truth in Lending Act, 16 U.S.C. 1601, *et seq.* (73 FR 1672, January 9, 2008). The proposed rule is intended to accomplish three goals: (1) To protect consumers in the mortgage market from unfair, abusive, or deceptive lending and servicing practices while preserving responsible lending and sustainable homeownership; (2) to ensure that mortgage loan advertisements provide accurate and balanced information and

do not include misleading or deceptive representations; and (3) to require earlier mortgage disclosures for non-purchase money mortgage transactions which would include mortgage refinancings, closed-end home equity loans, and reverse mortgages (73 FR 1672).

In its proposal, the Board would establish new protections for higher-priced mortgages, a newly defined category of loans, and for all mortgage loans. The proposed rule contains four key protections for higher-priced mortgage loans to prohibit creditors from: (1) Engaging in a pattern or practice of extending credit based on the collateral without regard to the consumer's ability to repay; (2) making a loan without verifying the income and assets relied upon to make the loan; (3) imposing prepayment penalties in certain circumstances; and (4) making loans without establishing escrows for taxes and insurance (73 FR 1673).

The Board also proposes, for all mortgage transactions, to prohibit creditors from paying mortgage brokers more than the consumer agreed the broker would receive. Specifically, the proposed rule would prohibit a creditor from making a payment, "directly or indirectly, to a mortgage broker unless the broker enters into an agreement with a consumer" (73 FR 1725). Further, a creditor payment to a mortgage broker could not exceed the total amount of compensation stated in the written agreement, reduced by any amounts paid directly by the consumer or by any other source (Id).

In proposing the mortgage broker agreement, the Board recognizes HUD's current policy statements and regulatory requirements regarding disclosure of mortgage broker compensation and noted that HUD had announced its intention to propose improved disclosures under RESPA (73 FR 1700). The Board stated that it intends that its proposal "* * * would complement any proposal by HUD and operate in combination with that proposal to meet the agencies' shared objectives of fair and transparent markets for mortgage loans and for mortgage brokerage services."

HUD believes its proposals regarding the GFE and mortgage broker compensation are consistent with those of the Board. As HUD moves forward to finalize this rule, it will continue to work with the Board to make the respective rules consistent, comprehensive, and complementary.

D. Planned Implementation of Final Rule

Given the significant changes that would be made in its RESPA regulations by this proposed rule, the Department intends to include a transition period in the final rule. During the 12-month transition period, settlement service providers and other persons may comply with either the current requirements or the revised requirements of the amended provisions. HUD is seeking comments on whether such a transition period is appropriate.

E. The GFE and GFE Requirements

Problems Identified with the Existing GFE. Under RESPA, loan originators must provide a GFE of the borrower's settlement costs (along with HUD's Special Information Booklet in home purchase transactions) at or within 3 days of a mortgage loan application. RESPA authorizes HUD to prescribe regulations concerning the GFE, and HUD's regulations at 24 CFR 3500.7, along with the suggested format set forth in Appendix C to the regulations, constitute the current GFE guidance. At the closing, a borrower must receive the Uniform Settlement Statement (HUD–1 or HUD–1A), which itemizes final settlement charges to borrowers. The regulations at 24 CFR 3500.8–3500.10 and the instructions in Appendix A to the regulations specify HUD's requirements for the HUD–1/1A.

HUD believes that the GFE could better facilitate borrowers shopping for the best loan. Further, the GFE could better achieve the statute's purposes of preventing unnecessarily high settlement costs by requiring a more accurate and consistent presentation of costs. The regulations do not require that the GFE be given to the borrower until after he or she submits a full application to an originator. This can result in a borrower paying significant fees before receiving a GFE, inhibiting the possibility of shopping beyond the provider with whom the applicant first applies. HUD's RESPA regulations require that the GFE include a list of charges but they do not prescribe a standard form. Consequently, it is virtually impossible to shop and compare the charges of various originators and settlement service providers using the GFE, because different originators may list different types or categories of charges, or may identify specific charges by different names, or both. The current regulations also do not require that the GFE contain information on the terms of loans, such as the loan's interest rate, for purposes of comparison. Further, while the HUD Special Information Booklet supplements the GFE, the GFE does not provide certain important explanatory information to the borrower including, for example, how the borrower can use the document to shop and compare loans. The GFE also does not make clear the relationship between the closing costs and the interest rate on a loan.

HUD's current regulations require loan originators to list on the GFE the "amount of or range of" each charge that the borrower is likely to incur in connection with the settlement.[6] The suggested GFE format, found in Appendix C to the regulations, lists 20 common settlement services. The suggested format also provides a space for listing any other applicable services and charges. These requirements have led, in many instances, to a proliferation of charges for separate "services" without any actual increase in the work performed by individual settlement service providers.

The RESPA regulations do not require that the GFE clearly identify the total charges of major providers of settlement services, including lenders and brokers (loan originators), title agents and insurers (title charges), and other third party settlement service providers. Without the simplification provided by presenting totals for major items, it is difficult for borrowers to know how much they are paying for major items, including origination and title related charges, or how they can compare loans and select among service providers to get the best value.

The estimated costs on GFEs are frequently unreliable or incomplete, or both, and final charges at settlement often include significant increases in items that were estimated on the GFE, as well as additional surprise "junk fees," which can add substantially to the consumer's ultimate closing costs.

New GFE Requirements. In light of these considerations, HUD believes that in order for the GFE to better serve its intended purpose, which is to apprise borrowers of the charges they are likely to incur at settlement, a number of specific changes to the GFE requirements are required to make it firmer and more useable. Accordingly, today's proposed rule would establish a new required GFE form to be provided to borrowers by loan originators in all RESPA covered transactions.[7] HUD

[6] 24 CFR 3500.7(a).

[7] HUD's RESPA rules currently provide that in the case of a federally related mortgage loan involving an open-end line of credit (home equity plan) covered under the Truth in Lending Act and Regulation Z, a lender or broker that provides the borrower with the disclosures required by 12 CFR

believes that the content of the material in the proposed form gives the consumer the information needed to shop for loan products and to assist them during the settlement process. The Department seeks public comment on the proposed GFE, as well as the proposed HUD–1/1A Settlement Statement forms. The following sections address the proposed changes, and, where appropriate, include a summary of comments received on the issue in response to the 2002 Proposed Rule, as well as comments voiced during the 2005 RESPA Reform Roundtables.

1. Changes to Facilitate Shopping

The Proposed Rule. Today's rule proposes to establish a new definition for a "GFE application" and a separate new definition for "mortgage application." The GFE application would be comprised of those items of information that the borrower would submit to receive a GFE. Such an application would include only such information as the originator considered necessary to arrive at a preliminary credit decision and provide the borrower a GFE. Specifically, a GFE application would include six items of information (name, Social Security number, property address, gross monthly income, borrower's information on the house price or best estimate of the value of the property, and the amount of the mortgage loan sought) in order to enable a loan originator to make a preliminary credit decision concerning the borrower. The proposed rule will also require that the GFE application be in writing or in computer-generated form. Oral applications can be accepted at the option of the lender. In such cases, the lender must reduce the oral application to a written or electronic record.

The proposed rule also provides that when a borrower chooses to proceed with a particular loan originator, the loan originator may require that the borrower provide a "mortgage application" to begin final underwriting. The mortgage application will ordinarily expand on the information provided in the GFE application, including bank and security accounts and employment information as well as asset and liability information and all the other information that the originator requires to underwrite the loan.

To facilitate shopping and lower the cost burden of shopping on consumers and industry alike, the proposed rule would not require that all underwriting information be supplied at the GFE application stage. Nevertheless, borrowers must be protected against "bait and switch." Accordingly, the proposed rule provides that during final underwriting, the originator may verify the information in and developed from the GFE application, including employment and income information, ascertain the value of the property to secure the loan, update the credit analysis, and analyze any relevant information collected in the entire application process, including, but not limited to, information on the borrower's assets and liabilities. However, borrowers may not be rejected unless the originator determines that there is a change in the borrower's eligibility based on final underwriting, as compared to information provided in the GFE application and credit information developed for such application prior to the time the borrower chooses the particular originator.[8] The originator must document the basis for any such determination and keep these records for no less than 3 years after settlement, in accordance with proposed subsection 24 CFR 3500.7(f)(1)(iii).

Where a borrower is rejected for a loan for which a GFE has been issued, and another loan product is available to the borrower, the loan originator must provide the borrower with a revised GFE. Where a borrower is rejected, the borrower must be notified within one business day and the applicable notice requirements satisfied.

Loan originators will provide GFEs based on the GFE applications that are memorialized in writing or electronic form. A separate GFE must be provided for each loan where a transaction will involve more than one mortgage loan. For loans covered by RESPA, Truth in Lending Act (TILA) disclosures would also be provided within 3 days of a written GFE application, unless the creditor, i.e., loan originator, determines that the application cannot be approved on the terms requested. (See comments 19(a)(1)–3 and 4 of the Federal Reserve Board's Official Staff Commentary on the Truth in Lending Act (TILA).) Based on consultations with representatives of the Federal Reserve, when a GFE application is submitted, an initial TILA disclosure should also be provided so long as the application is in writing, or, in the case of an oral application, committed to written or electronic form.

By obtaining multiple GFEs, borrowers will be in a position to decide which loan provider and which mortgage product they wish to select. When the borrower makes those decisions, the borrower will notify the originator, who may then require a more comprehensive "mortgage application," and possibly a fee or fees, to initiate the loan origination. As indicated, this application would consist of the more detailed information required by the originator, submitted in order to obtain a final underwriting decision, leading to origination of a mortgage loan.[9]

Discussion. Under RESPA, a GFE must be provided to a borrower at or within 3 days of application. HUD's current regulations define an application as the "submission of a borrower's financial information in anticipation of a credit decision, whether written or computer generated, relating to a federally related mortgage loan" identifying a specific property.[10] The 2002 Proposed Rule sought to make GFEs more readily available to consumers and, therefore, more useful as a shopping tool by clarifying the minimum information needed to obtain a GFE and by broadening the rules to allow oral applications, consistent with earlier informal interpretations by HUD, so long as such requests contained sufficient information for the originator to provide a GFE. Accordingly, the 2002 Proposed Rule also revised the definition of "application" in the regulations to make it clear that an application would be deemed to exist, and that the GFE should be provided once the consumer provided sufficient information to enable a loan originator to make an initial determination regarding the borrower's creditworthiness (typically, a Social Security number, a property address, basic income information, the borrower's information on the house price or best estimate of the value of the property, and the mortgage loan amount needed), whether orally, in writing or computer-generated. The GFE would be given to the borrower, conditioned on final loan approval following full underwriting and appraisal of the property securing the mortgage.

HUD acknowledged in the 2002 Proposed Rule that the proposed changes in the definition of "application" and the requirement that a GFE be provided to prospective borrowers early in the shopping process

226.5b of Regulation Z at the time the borrower applies for such loan shall be deemed to comply with GFE requirements set forth at 24 CFR 3500.7. Nothing in this proposed rule is intended to change this provision.

[8] Unforeseeable circumstances resulting in a change in the borrower's eligibility may also be a basis for rejecting the borrower. Unforeseeable circumstances are also discussed in Section 8(b) below.

[9] HUD anticipates that in most cases a mortgage application will be the Uniform Residential Loan Application, Freddie Mac Form 65, or Fannie Mae Form 1003.

[10] 24 CFR 3500.2.

might have implications for the content and delivery of required disclosures under TILA requirements. As a result, HUD invited comments on how the proposed GFE changes might impact other disclosure requirements, and also invited comments on how the proposed GFE changes could be harmonized with the other disclosure requirements.

As indicated above, under today's proposal, the definition of "GFE application" provides the trigger for initial RESPA disclosures. After a consumer decides to proceed with a particular loan originator's GFE, the loan originator will generally require a separate "mortgage application" as defined under this proposed rule, before making a credit decision. Consumer representatives recommended that HUD consult with the Federal Reserve Board to coordinate the timing of RESPA and TILA disclosures. Industry commenters on the 2002 Proposed Rule were generally concerned that HUD's proposal to require disclosures earlier in consumers' process of shopping for a mortgage would trigger requirements under the Home Mortgage Disclosure Act (HMDA) and the Equal Credit Opportunity Act (ECOA).

By refining the definition of "application" under RESPA, and dividing the application process as described, HUD believes that today's proposal will facilitate the availability of shopping information and avoid unnecessary regulatory burden on the industry and an unwarranted increase in notices of loan denials to borrowers. Whether a GFE application under a particular set of facts triggers HMDA or ECOA requirements must be determined under Regulation B and Regulation C, as interpreted in the Federal Reserve Board's official staff commentary. It should be noted that by proposing such a change to the current definition of "application," HUD does not intend to prevent a loan originator from prequalifying a borrower for a mortgage loan.

2. Addressing Up-Front Fees That Impede Shopping

The Proposed Rule. The proposal would allow a loan originator, at its option, to collect a fee limited to the cost of providing the GFE, including the cost of an initial credit report, as a condition for providing a GFE to the prospective borrower.

Discussion. HUD would prefer that originators not impose any charges for a GFE, since providing a GFE before the payment of any fee will further facilitate shopping. HUD believes it would be reasonable for loan originators to treat shoppers for mortgages in much the same way other retailers treat shoppers, where the price of the product includes marketing expenses and purchasers pay the cost incurred to serve shoppers who do not purchase the goods or services. Such an approach would better serve the purposes of the statute. However, HUD recognizes that there may be incidental or nominal costs to provide GFEs to prospective borrowers. Therefore, in order to facilitate shopping using GFEs, the proposed rule would allow a loan originator, at its option, to collect a fee limited to the cost of providing the GFE, including the cost of an initial credit report, as a condition for providing a GFE to a prospective borrower. HUD is interested in receiving comments on this approach.

3. Introductory Language

The Proposed Rule. The proposed GFE explains to the borrower: (1) The purpose of the GFE, i.e., that it is an "* * * estimate of your settlement costs and loan terms if you are approved for this loan" and (2) informs the borrower that he or she is the "* * * only one who can shop for the best loan for you. You should compare this GFE with other loan offers. By comparing loan offers, you can shop for the best loan."

Discussion. The GFE proposed today informs the borrower that he or she is the only one who can shop for the best loan. HUD believes that this formulation should be useful to consumers dealing with all types of loan originators.

The 2002 Proposed Rule had included language in this section of the previously proposed GFE that was intended to describe the role of the loan originator and to encourage borrowers to shop for themselves. Comments both from consumer groups and industry generally favored removing language on the GFE that discussed the role of the loan originator, on the grounds that the language was misleading, confusing, and might conflict with state law. AARP, however, supported retaining the portion of the proposed language that encourages the borrower to shop among loan originators.

In light of the comments received on the 2002 proposal, today's proposed GFE does not include any language on the role of the loan originator. Instead, the language on the proposed GFE informs the consumer that he or she is the only one who can shop for the best loan.

4. Terms on the GFE (Summary of Loan Details)

The Proposed Rule. The proposed GFE includes a summary of the key terms of the loan. The form discloses the initial loan amount; the loan term; the initial interest rate on the loan; the initial monthly payment owed for principal, interest, and any mortgage insurance; and the rate lock period. The form also discloses whether the interest rate can rise, whether the loan balance can rise; whether the monthly amount owed for principal, interest and any mortgage insurance can rise; whether the loan has a prepayment penalty or a balloon payment and whether the loan includes a monthly escrow payment for property taxes and possibly other obligations. HUD is requiring the terms "prepayment penalty" and "balloon payment" to be interpreted consistent with TILA (15 U.S.C. 1601 *et seq.*). The Annual Percentage Rate (APR) is not included on the proposed GFE.

Discussion. One of HUD's objectives in proposing revisions to the current RESPA regulations is to ensure that consumers are able to use page one of the GFE to comparison shop among loan originators for a mortgage loan. Accordingly, page one of the proposed GFE contains a summary of the loan terms and details, as well as a summary of the total estimated settlement charges for the loan. The new summary format of page one of the proposed GFE with its list of important loan terms will increase consumer awareness and allow borrowers the opportunity to shop among loan originators and easily compare various loan offers.

The proposed GFE is designed to provide clear information on both fixed and adjustable rate mortgages. The disclosure of terms on the latter is complicated due to their variable structure and to future changes in interest rates. Adjustable rate mortgages have recently experienced high default rates. HUD seeks comment on possible additional ways to increase consumer understanding of adjustable rate mortgages.

The 2002 proposed GFE advised the borrower of the terms of the mortgage and included the interest rate and the APR. It also advised the borrower whether or not the loan had a prepayment penalty or balloon payment, and whether the loan had an adjustable rate and, if so, its terms. Comments on the 2002 GFE primarily concerned whether it should include information also appearing on the TILA disclosure. Consumers generally supported the inclusion of TILA disclosure information on the GFE. Lenders generally recommended that information appearing on TILA disclosures should be removed from the GFE because borrowers will continue to receive separate TILA disclosure forms, and inclusion on the GFE is unnecessary and would potentially lead

to borrower confusion. Some participants at the RESPA Reform Roundtables suggested that more information on new loan products such as interest-only loans should be included on the GFE.

While mindful of the need to present consumers with key loan information on the GFE, HUD has determined not to include the APR on today's proposed GFE. The APR is central to the TILA disclosure that will be provided in purchase transactions at the same time as the GFE and ordinarily at the same time in other transactions. However, the terms "prepayment penalty" and "balloon payment" have been retained on the form to facilitate consumer shopping, even though these terms are also included on the TILA disclosure.

With respect to today's proposed GFE, HUD notes that there are differences between how the GFE discloses the monthly payment and how the TILA form will disclose the monthly payment. Specifically, the proposed GFE requires disclosure of principal, interest, and any mortgage insurance, while the TILA disclosure may include amounts for taxes. HUD will revise its Special Information Booklet to explain this difference, to avoid consumer confusion.

The interest rate listed on the GFE will reflect the loan offered at the time the GFE is given. Until locked in, the interest rate will float. For loans originated by mortgage brokers, the amount of any "charge or credit to the borrower for the specific interest rate chosen" will float with the wholesale market.[11] This is because mortgage brokers must report the precise difference between the price of the loan and its par value in the "charge or credit for the specific interest rate chosen." As a result, borrowers who use brokers as defined in this proposed rule and choose to float will float according to wholesale lenders' changes.

Current federal regulations allow originators to provide GFE and TILA information together.[12] However, the proposed GFE is designed as a distinct, required form to promote shopping by consumers. HUD believes it is best complemented by providing a separate TILA disclosure along with the GFE.

5. Period During Which the GFE Terms Are Available to the Borrower

The Proposed Rule. The interest rate stated on the GFE would be available until a date set by the loan originator for the loan. After that date, the interest rate, some of the loan originator charges, the per diem interest, and the monthly payment estimate for the loan could change until the interest rate is locked. The estimate of the charges for all other settlement services would be available until 10 business days from when the GFE is provided, but it may remain available longer, if the loan originator extends the period of availability.

Discussion. In order to promote competition while avoiding committing originators to open-ended offers, the 2002 Proposed Rule would have required that the GFE be held open for a minimum of 30 days. Commenters on the 2002 Proposed Rule were specifically asked whether 30 days was an appropriate period, and considerable comment was elicited on this subject. A major consumer group supported the 30-day period, while the majority of lenders commenting on the 2002 proposal recommended a 10-day shopping period or less.

Today's proposed rule reflects HUD's determination that the appropriate period for which GFE terms are generally to be available is 10 business days, excluding the interest rate of the loan set forth in the GFE, some of the loan origination charges related to the interest rate, the per diem interest, and the monthly payment estimate. The interest rate stated on the GFE would be available until a date set by the loan originator for the loan. After that date, the interest rate, some of the loan originator charges, the per diem interest, and the monthly payment estimate for the loan could change until the interest rate is locked.

A central purpose of RESPA regulatory reform is to facilitate shopping in order to lower settlement costs, and there is legitimate concern that requiring GFEs to be open for too long a shopping period could unintentionally operate to increase borrower costs. By requiring that the GFE terms be generally available for 10 business days, GFEs will be effectively open for 2 weeks, thereby providing borrowers with sufficient time to shop among various offers and providers. Borrowers may request, and originators at their option may lengthen the shopping period for a loan or loans beyond 10 business days. In such cases, the originator should note and initial the increased duration the GFE is open on the borrower's GFE.

6. Consolidating Major Categories on the GFE

The Proposed Rule. The proposed GFE would group and consolidate all fees and charges into major settlement cost categories, with a single total amount estimated for each category.

Discussion. Under current RESPA rules, the GFE simply lists estimated charges or ranges of charges for settlement services. There is no requirement for grouping or subtotaling charges to the same recipients. The costs listed on the GFE include loan originator charges such as loan origination and underwriting charges; charges by third parties for lender-required services, such as appraisal, title, and title insurance fees; state and local charges imposed at settlement such as recording fees or city/county stamps; and amounts the borrower is required to put into an escrow account, or reserves, for items such as property taxes or hazard insurance. At settlement, borrowers receive a second RESPA disclosure—the Uniform Settlement Statement (the HUD–1/1A) that enumerates the final costs associated with both the loan and, if applicable, the purchase transaction.

The proposed GFE would group and consolidate all fees and charges into major settlement cost categories, with a single total amount estimated for each category. This approach would reduce any incentive for loan originators and others to establish a myriad of "junk fees" and provide them in a long list in order to increase their profits.

In the 2002 Proposed Rule, HUD had proposed a GFE that grouped and consolidated charges into major cost categories, with a single total amount for each category. In commenting on the 2002 proposal, consumer groups were split on the best approach to addressing fee proliferation on the GFE. AARP strongly supported consolidation of major cost categories, and recommended that HUD's proposed categories be further consolidated into three categories for enhanced consumer comprehension. The National Consumer Law Center (NCLC) filed comments on its own behalf, and on behalf of the Consumer Federation of America, National Association of Consumer Advocates, Consumers Union, and U.S. Public Interest Research Group. These commenters noted that while subtotaling is helpful to consumers, itemization on the HUD–1 is necessary to ensure that compliance with TILA and the Home Ownership and Equity Protection Act (HOEPA) can be determined. The National Community Reinvestment Coalition and the National Center on Poverty Law indicated their belief that the

[11] The "charge or credit for the interest rate chosen" concerns the discount points and the yield spread premium that are further discussed in Section C of this preamble.

[12] 24 CFR 3500.7(d).

tolerance [13] levels will address the issue of proliferation of fees, and commented that the GFE must be as similar as possible to the HUD–1 for comparison purposes. Lenders who commented on this proposed change to the GFE in 2002 expressed concern that lumping costs together in large categories will confuse consumers when they compare data on the GFE with data on the HUD–1/1A.

Having considered the results of consumer testing of the forms as detailed below in Section F and comments received on the 2002 Proposed Rule, HUD has determined to propose a standardized GFE, containing major cost categories, to facilitate better borrower understanding of settlement services and their costs, and empower borrowers to shop, compare, and negotiate major cost items where possible. HUD is not proposing to further consolidate the categories, because it believes that each of the proposed categories provides useful information to borrowers. Although today's proposed GFE does not itemize the services required in each category, it does explain to the borrower the exact nature of each category of services. For example, origination services are characterized as the services and charges to obtain and process the loan for the borrower. HUD also regards the information on required services that can and cannot be shopped for as useful information that borrowers should have in choosing an originator and later to facilitate shopping for services to lower costs.

HUD's current RESPA regulations require that the GFE include a list of any lender-required providers, including the name, address and telephone number of the provider and the nature of the lender's relationship with the provider. Under today's proposed rule, if the lender requires the use of a particular provider other than its own employees, and requires the borrower to pay any portion of such service, the lender must identify on the GFE the service, and the estimated cost or range of charges for the service. HUD has determined to eliminate the requirement to identify the name of the required service provider, because it believes that consumers will use the GFE to shop among loan originators based on cost rather than on the identity of individual settlement service providers.

Where a lender permits a borrower to shop for a required settlement service, under today's proposed rule the lender must provide the borrower with a written list of identified providers at the time the GFE is provided. Such a list may be included on the GFE form or on a separate sheet of paper.

The GFE set forth in the 2002 Proposed Rule would also have referenced the corresponding series on the HUD–1, to facilitate comparison between the GFE and HUD–1. While these references have been removed in the GFE proposed today in the interest of simplifying the form, HUD is also proposing changes to the HUD–1/1A to facilitate comparison of the GFE to the HUD–1/1A. Section II.D. of this preamble discusses today's proposed changes to the HUD–1/1A.

Pursuant to 24 CFR 3500.15, originators seeking to satisfy the requirements for the affiliated business exemption must provide the requisite affiliated business arrangement disclosure at the time of any referral to an affiliated settlement service provider. The GFE proposed by today's Proposed Rule does not attempt to include this information. However, under HUD's existing RESPA regulations, the affiliated business disclosure must be given on a separate form consistent with Appendix D of HUD's existing regulations. Where such a referral occurs at the time a GFE is given, the affiliated business disclosure must be given along with the GFE.

7. Option to Pay Settlement Costs

The Proposed Rule. The GFE Form shall advise the borrower how the interest rate of the loan affects the borrower's settlement costs, and shall include actual available options in this regard on the form.

Discussion. In addressing the problem of lender payments to mortgage brokers in the 1999 and 2001 Policy Statements,[14] HUD made it clear that consumers should be advised as early as possible when shopping for a loan of how their interest rate affects their settlement costs and that their options in this regard should be presented on the GFE form. In order to decide which rate/cost combination is best, HUD regards it as essential that borrowers be presented actual offers of the loan originator on the chart on page 3 of today's proposed GFE. The GFE would inform borrowers that: (1) They can choose the loan presented in the GFE; (2) they can choose an otherwise identical loan with a lower interest rate and monthly payments that will raise settlement costs by a specific amount; or (3) they can choose an otherwise identical loan with a higher interest rate and monthly payments that will lower settlement costs by a specific amount. If a higher or lower interest rate is not in fact available from the originator, the originator must provide those options that are available and indicate "not available" on the form for those options that are not available. While some commenters on the 2002 Proposed Rule recommended that HUD require loan originators to feature specific types of loans on the loan option chart on the GFE, HUD does not believe that it should impose requirements on loan originators on what types of loans are offered to borrowers. Therefore, HUD does not propose such requirements in today's proposed rule. HUD's consumer testing has demonstrated that consumers responded very positively to the trade-off chart on the GFE that presents information on different interest rates and up-front fees. In fact, this was the feature that consumers liked best about the form.

The provision of this information on page 3 of the form will help borrowers understand their options for paying settlement costs. If the borrower chooses one of the two alternative options presented on the form, the borrower must receive a new GFE.

8. Establishing Meaningful Standards for GFEs

a. Tolerances.

The Proposed Rule. The proposal would prohibit loan originators from exceeding at settlement the amount listed as "our service charge" on the GFE, absent unforeseeable circumstances. The charge or the credit to the borrower for the interest rate chosen, if the interest rate is locked, absent unforeseeable circumstances, also cannot be exceeded at settlement. The proposal would also prohibit Item A on the GFE, "Your Adjusted Origination Charges" from increasing at settlement once the interest rate is locked. In addition, the proposal would prohibit government recording and transfer charges from increasing at settlement, absent unforeseeable circumstances. The proposal would prohibit the sum of all the other services subject to a tolerance (originator required services where the originator selects the third party provider, originator required services where the borrower selects from a list of third party providers identified by the originator, and optional owner's title insurance, if the borrower uses a provider identified by the originator) from increasing at settlement by more than 10 percent absent unforeseeable

[13] "Tolerance" refers to the maximum amount by which the charge for a category of settlement costs may exceed the amount of the estimate for such category on a GFE, and is expressed as a percentage of an estimate. See Section (h) below.

[14] 64 FR 10080 (March 1, 1999), 66 FR 53052 (October 18, 2001).

circumstances. Thus, a specific charge may increase by more than 10 percent at settlement, so long as the sum of all the services subject to the 10 percent tolerance does not increase by more than 10 percent.

Discussion. Current RESPA regulations at 24 CFR 3500.7(a) require a lender to provide a "good faith estimate" of the "amount of or range of charges for the specific settlement services the borrower is likely to incur in connection with the settlement." While the rules require that the estimate be made "in good faith" and "bear a reasonable relationship" to the charges the borrower is likely to incur at settlement, HUD is proposing to clarify what a "Good Faith Estimate" demands, both with regard to the loan originator's own charges, as well as to lender-selected, third party charges and other settlement costs.

Estimates appearing on the GFEs can be significantly lower than the amount ultimately charged at settlement and do not provide meaningful guidance on the costs borrowers will incur at settlement. While unforeseeable circumstances can drive up costs in particular circumstances, in most cases loan originators have the ability to estimate final settlement costs with great accuracy. The loan originator's own charges, which are entirely within the originator's control, can be stated with certainty, absent unforeseeable circumstances. Government recording and transfer charges are well known to loan originators or can be calculated based on the purchase price or value of the property. Moreover, many third party costs such as credit report fees, pest inspection fees, tax services, and flood reviews are readily ascertainable. Other third party costs such as title services and title insurance and up-front mortgage insurance premiums, typically only vary depending on the value of the property or the loan amount. HUD also is aware that recent advances in technology and telecommunications in loan processing make routine provision of accurate estimates of third party costs easier and cheaper.

Some borrowers have indicated that the GFE has often failed to represent an accurate estimate of final settlement costs, for a number of reasons. In too many cases, fees that were not included on the GFE materialize at settlement. These unexpected fees often result in extra compensation for the originator and/or the third party settlement service providers and in higher charges to the borrower. The absence of more precise regulatory standards for providing a good faith estimate of final settlement costs has not helped ensure greater accuracy and reliability.

In light of these considerations, HUD believes that in order for the GFE to serve its intended purpose, which is to apprise prospective borrowers of the charges they are likely to incur at settlement, new standards must be established under existing law to better define good faith" and the standards applicable to the GFE.[15] Accordingly, the proposed rule states that loan originators may not increase their own charges (the service charge) from that stated on the GFE, absent "unforeseeable circumstances." Government recording and transfer charges would also not be able to increase at settlement, absent "unforeseeable circumstances." While the interest rate is locked, the charge or the credit to the borrower for the interest rate chosen also cannot be exceeded at settlement, absent "unforeseeable circumstances." While fees for the service charge have a "zero tolerance" under the proposed rule, absent unforeseeable circumstances, the sum of all the other services subject to a tolerance—required services the loan originator selects, title and closing services, lender's title insurance and optional owner's title insurance if chosen or identified by the originator, and required services that borrowers can shop for when the borrower elects to use the provider identified by the originator—would be subject to a single overall 10 percent tolerance. Thus, a specific charge may increase by more than 10 percent, so long as the total does not increase by more than 10 percent.

The subject of tolerances received considerable attention from commenters in the 2002 proposed RESPA rulemaking, as well as during the RESPA Reform Roundtables. Generally, lending industry groups commenting on the 2002 Proposed Rule opposed tolerances on the grounds that settlement costs are extremely variable and subject to change after appraisal and underwriting. Many other comments from lenders on the 2002 Proposed Rule noted that costs often change after property appraisal and as a result of borrower product changes or changes in the loan amount or closing date. Consumer groups, on the other hand, supported tolerances as a means to prevent "bait and switch" tactics by loan originators. Regulators, including the Conference of State Bank Supervisors and the American Association of Residential Mortgage Regulators, were generally supportive of tolerances. During the RESPA reform roundtables, many participants who expressed comments on the need for tolerances agreed that it is possible to get solid estimates of costs at the GFE stage, while others expressed concern that a 10 percent tolerance level is too strict.

In its written comments in response to the 2002 Proposed Rule, the American Land Title Association (ALTA) questioned HUD's authority to adopt tolerances in light of the legislative history of the good faith estimate requirement in Section 5(c) of RESPA. ALTA noted that as part of the original RESPA statute, Congress enacted a separate section that required lenders, at the time of loan commitment, but not later than 12 days prior to settlement, to provide the prospective buyer and seller with an "itemized disclosure in writing of each charge arising in connection with the settlement." Section 6 of the original statute imposed a duty on the lender to obtain from persons who were to provide services in connection with the settlement "the amount of each charge they intend to make." If the exact charge was not available, a good faith estimate could be provided. Section 6(b) provided for lender liability to the buyer or seller for failure to provide the requisite disclosures in the amount of actual damages or $500, whichever was greater, and, if the action was successful, attorney's fees and court costs.

ALTA noted that due to concerns raised by lenders about Section 6, that provision of RESPA was repealed within one year of enactment. Congress substituted for Section 6 the language of Section 5(c) requiring lenders to provide a good faith estimate of settlement costs, along with a Special Information Booklet, within 3 days of loan application. ALTA also noted that Congress did not impose any sanctions for violations of the Section 5(c) obligation. In light of this legislative history, ALTA contends that HUD does not have statutory authority to adopt tolerances as proposed.

While mindful of the legislative history of RESPA with respect to the enactment and later repeal of the section requiring lenders to provide disclosures of the amount of each charge arising in

[15] Differing editions of Black's Law Dictionary have defined "good faith" as a "state of mind consisting in * * * honesty in belief or purpose * * * and faithfulness to one's duty or obligation," and "freedom from knowledge of circumstances which ought to put the holder upon inquiry," as well as "absence of all information, notice, or benefit or belief of facts which render a transaction unconscientious." Inherent in these definitions is the concept that where a party makes an estimate in good faith, the party will take into account all available relevant information, and will exercise reasonable care in evaluating such information before providing such an estimate.

connection with the settlement, HUD believes that the tolerance approach it is proposing today is distinguishable from the requirement to provide an itemized disclosure of each charge. Unlike the requirement in the original Section 6 of RESPA that required lenders to provide exact figures for individual settlement charges, today's proposed approach permits considerable flexibility. The proposal would permit all charges to decrease between the time the GFE is provided and the date of settlement; all charges may increase in the event of unforeseeable circumstances; and some third party charges such as homeowners' insurance are not subject to any tolerance. Moreover, individual charges for certain third party services that originators require and either select or identify may increase by more than 10 percent at settlement, as long as the sum of such charges increases by no more than 10 percent at settlement.

In considering the appropriate tolerance for third party settlement services on the GFE, HUD considered the available data on the variation in the cost of title services within individual market areas. Title services is the largest component of third party settlement service costs, accounting for slightly over two-thirds of the total among the sample of Federal Housing Administration (FHA) insured-loans discussed in the Economic Analysis. A study by Consumers Union on the dispersion of title costs within each of five large California metropolitan areas provides the best available data. Consumers Union found that, for four of the five metropolitan areas—Los Angeles, San Francisco, San Diego, and Sacramento—the highest reported prices for title services were between 9.95 percent and 13.84 percent above the average price in the local market. The exception is Fresno, where the highest price is 27.90 percent above the average. These data indicate that a title insurance company should be able to remain within about 10 percent of its originally quoted price, in the event that a particular loan turns out to involve more extensive title work than originally anticipated. HUD therefore has concluded that a 10 percent tolerance is reasonable. To provide a further margin for unexpected cost increases, HUD extended the 10 percent tolerance per service in the 2002 Proposed Rule to a 10 percent tolerance for the combined total cost of all third party settlement services selected by the lender. Other services are a much smaller share of the total cost of third party settlement services, and therefore increases in their cost are likely to have a much smaller impact on the combined total cost of all third party settlement services covered by the 10 percent tolerance.

The proposal also clarifies that if the borrower requests a change in the type of loan, loan amount, or loan product, or otherwise makes a change to the mortgage transaction, the originator is not bound by the original GFE. However, because the borrower is in effect initiating a new application, today's proposed rule would require that the originator must either adhere to the original GFE or must redisclose to the borrower by providing a new GFE, and the originator would then be subject to the tolerances applicable to that GFE, provided the originator chooses to accommodate the change and the borrower qualifies for the change.

In addition, to meet the tolerances, today's proposed rule provides that originators must include all charges correctly within their prescribed category on the GFE (and the HUD-1/1A). This means that third party fees estimated on the GFE must be reported as the estimated prices to be paid to third parties only, and fees reported on the HUD-1/1A must not exceed those actually paid to third parties, except where the prices are based on an average calculated in accordance with proposed § 3500.8(b)(2). (See Section G discussion on average cost pricing in this preamble.)

While loan originators are expected to issue a GFE of settlement costs where a borrower submits a GFE application, in the case of new construction, settlement costs can change between the time a purchase contract is signed and settlement. Such estimates are subject to the provisions regarding unforeseeable circumstances and the provision for borrower requested changes, including the documentation requirements discussed below. The proposed rule provides that the loan originator may provide the GFE to the borrower with a clear and conspicuous disclosure stating that at any time up until 60 days prior to closing, the loan originator may issue a revised GFE. If no such disclosure is provided with the initial GFE, the loan originator would not be able to issue a revised GFE except as otherwise provided in the rule.

b. Unforeseeable Circumstances

The Proposed Rule. The proposal provides that loan originators should not be held to tolerances where actions by the borrower or circumstances concerning the borrower's particular transaction result in higher costs that could not have reasonably been foreseen at the time of the GFE application, or where other legitimate circumstances beyond the originator's control result in such higher costs. The proposal also provides that if unforeseeable circumstances result in a change in the borrower's eligibility for the specific loan terms identified in the GFE, the borrower must be notified of the rejection for the loan and be provided a new GFE if another loan is made available.

Discussion. While tolerances are necessary to provide "bright line" standards for consumers and industry alike, HUD recognizes that there may be circumstances under which loan originators should not be held to tolerances. The proposed rule details the circumstances under which tolerances may not apply, but indicates further that if it is possible for the loan originator to perform at all in such circumstances, the loan originator's charges may increase only to the extent caused by the particular circumstances.

Today's proposed rule defines "unforeseeable circumstances" as either: (1) Acts of God, war, disaster, or other type of emergency that makes it impossible or impracticable for the originator to perform; or (2) circumstances that could not be reasonably foreseen at the time of the GFE application, that are particular to the transaction and that result in increased costs, such as a change in the property purchase price, boundary disputes, or environmental problems that were not described to the loan originator in the GFE application; the need for a second appraisal; and flood insurance. As with any business transaction, the borrower has the ability to call off the transaction in such circumstances. The proposed rule specifically excludes market fluctuations from being regarded as unforeseeable circumstances.

Where an originator cannot perform or meet the tolerances because of unforeseeable circumstances, the originator must document the costs occasioned by the unforeseeable circumstances, and, as indicated, charge the borrower only the increased costs caused by such circumstances. Additionally, as indicated, when an increase in costs is necessary because of unforeseeable circumstances beyond the originator's control, the borrower should be notified within 3 days of such charges—as though a new application was filed—before any additional costs are incurred, and a new GFE reflecting the charges must be provided to the borrower. Finally, when unforeseeable circumstances result in a change in a borrower's eligibility for the loan identified in the GFE, the borrower

should be notified within one business day of the decision to reject the loan, and, if another loan is made available to the borrower, a new GFE must be provided to the borrower. In all cases, the loan originator must retain appropriate documentation explaining any unforeseeable circumstances for a transaction for no less than 3 years after settlement.

9. Important Information for Borrowers

Page 4 of the GFE provides important information for the borrower, including information on how to apply for the loan set forth in the GFE. Page 4 also informs borrowers that they may wish to consult government publications about loans and settlement charges that have been published by HUD and the Federal Reserve Board. In addition, Page 4 provides important information to borrowers about their financial responsibilities as homeowners. This section of the GFE notifies the borrower that in addition to the monthly loan payment for principal, interest, and mortgage insurance, the borrower will be required to pay other annual charges to keep the property. The section provides the borrower with an estimate for annual property taxes, along with homeowner's flood, and other required property protection insurance, but estimates for other annual charges such as homeowner's association fees or condominium fees are not required to be provided on the form. The section informs the borrower that the borrower may have to identify such other charges and ask for additional estimates from other sources. The section also states that such charges will not change based on the loan originator chosen by the borrower and advises the borrower not to consider the loan originator's estimates of such charges, when shopping for the best loan.

Page 4 also notes that lenders can receive additional fees from other sources by selling the loan at some future date after settlement. However, the borrower is informed that once the loan is obtained at settlement, the loan terms, the borrower's adjusted origination charges, and total settlement charges cannot change.

Page 4 also includes a mortgage shopping chart that allows borrowers to compare GFEs from different loan originators.

10. Enforcement

The Proposed Rule. Today's proposed rule provides that charging a fee in excess of the tolerance, or any other failure to follow the GFE requirements, constitutes a violation of Section 5 of RESPA. As discussed below, HUD is also considering a provision that would allow loan originators a limited period of time to remedy any potential violations of the tolerances established under the rule, and thereby ease their possible exposure to liability for such violations.

Discussion. In enacting RESPA, Congress sought to protect consumers from unnecessarily high settlement charges. Accordingly, HUD believes that charging of a fee in excess of the tolerance, or other failure to follow the GFE requirements, constitutes a violation of Section 5 of RESPA.

HUD is soliciting comments on whether to add a provision to HUD's regulations that would allow loan originators, for a limited time after closing, to address the failure to comply with tolerances under HUD's GFE requirements, and if so, how such a provision should be structured. HUD is considering providing in the final rule that if, within a specified period (such as 14 business days) after the closing, a loan originator identifies a charge that exceeded the tolerance and repays the excess amount of the charge to the consumer within the specified period, the loan originator would be in compliance with Section 5. HUD is interested in commenters' views on whether such a procedure would be useful, and if so, what would be the appropriate time frame for finding and refunding excess charges. HUD is also soliciting comments on whether such a provision could be abused and therefore harmful to consumers, and whether the ability of prosecutors to exercise enforcement discretion obviates the need for such a provision.

F. Lender Payments to Mortgage Brokers—Yield Spread Premium (YSP)

Background. Lenders routinely provide the funds for mortgages that mortgage brokers originate for borrowers. Mortgage brokers also may be compensated for their services in originating the mortgage by the borrower and/or the lender. When the interest rate on the loan exceeds the par interest rate of the lender, the lender pays the broker at closing an amount in excess of the principal amount of the loan, and this excess is commonly referred to in the mortgage industry as a "yield spread premium" (YSP). For the past decade, such payments have been the subject of numerous lawsuits and consumer complaints, typically because consumers claim they were unaware that their broker was receiving such compensation, in addition to the direct compensation they paid the broker. Moreover, these consumers assert that such payments resulted from their being placed in mortgages with higher than necessary interest rates without their knowledge. Some consumer advocates have argued that all such payments should be treated as referral fees or kickbacks and thus should be illegal per se under RESPA.

HUD has taken the position, however, that YSPs can be useful and should remain available as an option for mortgage borrowers to help pay their closing costs, particularly those borrowers with limited available cash who choose to pay some or all closing costs through a higher interest rate. HUD made its position on the issue clear in HUD's Policy Statement 2001-1 (2001 Policy Statement).[16] In the 2001 Policy Statement, HUD restated its view[17] that as long as the broker's compensation is for services, and total compensation is reasonable, interest rate-based lender payments to the mortgage broker are legal under RESPA. HUD did not mandate new disclosure requirements in the 2001 Policy Statement, but did commit itself to making full use of its regulatory authority to establish clearer requirements for disclosure of mortgage broker fees, and to improve the settlement process for lenders, mortgage brokers, and consumers.[18] In the 2001 Policy Statement, HUD stressed that disclosure of broker compensation was "extremely important and that many of the concerns expressed by borrowers over YSPs can be addressed by disclosing YSPs, borrower compensation to the broker, and the terms of the mortgage loan, so that the borrower may evaluate and choose among alternative loan options."[19] In brief, it has been HUD's consistent position that the existence of a YSP in any loan should be at the borrower's choice, based upon a complete understanding of the trade-off between up-front settlement costs and the interest rate.

HUD's current RESPA regulations require that a rate-based payment from a lender to a broker be reported on the GFE, and later on the HUD–1. Such payments are frequently characterized on the GFE and HUD–1 as a "YSP" or "yield spread premium," and then are designated as a "paid outside closing"

[16] Real Estate Settlement Procedures Act Statement of Policy 2001–1, Clarification of Statement of Policy 1999–1 Regarding Lender Payments to Mortgage Brokers, and Guidance Concerning Unearned Fees under Section 8(b), published October 18, 2001, at 66 FR 53052.

[17] 66 FR 53052.

[18] 66 FR 53052.

[19] 66 FR 53056.

or "POC."[20] The YSP is not often understood by the borrower. In addition, it is not listed as an expense to the borrower. At the same time, many brokers hold themselves out as shopping among various funding sources for the best loan for the borrower, and do not explain to the borrower that the payment they receive from the lender is derived from the borrower's interest rate. Some may even assert that the YSP is not a payment the borrower needs to be concerned with. The 2001 Policy Statement emphasized that earlier disclosure and the entry of yield spread premiums, as credits to borrowers would "offer greater assurance that lender payments to mortgage brokers serve borrowers' best interests."[21]

2002 Proposed Rule. The 2002 Proposed Rule provided that on the GFE, all brokers first disclose their total compensation charges and disclose any YSP as a lender payment to the borrower and discount points as additional borrower payments. The amounts of any lender payment or discount points would be combined with the total origination charges, to arrive at a net origination charge. It was this final figure that was to be emphasized and highlighted for borrower comparison among lenders and brokers.

The purpose of these changes in the GFE disclosure requirements, as proposed by the 2002 Proposed Rule, was to: (a) Make the borrower aware of the fact that the lender payments were a part of total origination costs, since they were directly related to the borrower's choice of a higher interest rate and monthly payment; (b) ensure that these payments worked to reduce out of pocket costs of the borrower; and (c) encourage the borrower to compare net origination costs of all loans whether from a lender or a broker, in order to select the loan product that best meets the borrower's needs. The rationale for the disclosure changes was to promote transparency, reduce borrower confusion, facilitate shopping, and, at the same time, avoid giving any competitive advantage to brokers or lenders in the marketplace.

Nearly all commenters on the 2002 Proposed Rule that discussed YSPs other than individual mortgage brokers or their national and state associations expressed support for greater broker fee disclosure. Consumer representatives, in particular, were strong supporters of disclosure along the lines that HUD proposed, and offered suggestions for making the requirements more enforceable. Consumer groups recounted the class action litigation that resulted from the payment of yield spread premiums and HUD's past statements committing the Department to ensuring better disclosure of yield spread premiums. The National Consumer Law Center (NCLC) said that to date, yield spread premiums are generally paid by the lender solely as compensation for a higher interest rate loan. In most cases, according to NCLC, the borrower is not only paying an up-front fee, but is also paying a higher interest rate as a result of being steered into above-par loans. Consumer groups asserted that the YSP should be defined for the consumer in simple, easy-to-understand language on the GFE.

Lenders and their trade groups, on the other hand, tended to favor HUD's requiring a separate Mortgage Broker Fee Agreement, as proposed by the lending industry in the last few years, which would be entered into by brokers and their customers, in addition to the GFE.

Mortgage brokers and their trade groups expressed vigorous opposition to disclosing the YSP as a credit to the borrower. They maintained that such a characterization is misleading, unfair, and anti-small business. The brokers stated that HUD's proposal: (1) Created confusion for the borrower; (2) would unnecessarily increase HOEPA transactions; (3) would stifle FHA and low/moderate-income lending; (4) would unfairly target brokers; (5) would create an uneven playing field with retail lenders; and (6) could adversely affect tax treatment of borrowers.

FHA Issue. Currently, FHA regulations limit origination fees for loans insured under the FHA program generally to one percent of the mortgage amount (see 24 CFR 203.27(a)(2)(i)). FHA does not have authority under the National Housing Act (12 U.S.C. 1709(b)(2)) to limit payments between loan originators, and yield spread premiums are not included in calculating the FHA limits on origination fees. Some industry commenters argued that the YSP disclosure, as proposed in 2002, would have adversely affected the origination of FHA loans. Specifically, the National Association of Mortgage Brokers (NAMB) commented that if the 2002 Proposed Rule were finalized, many mortgage brokers would cease to originate FHA loans because of the origination fee limitation. The MBA and some of its member firms argued for removal or adjustment of the FHA origination fee cap.

RESPA Roundtables. At the 2005 RESPA Reform Roundtables, consumer representatives generally continued to support disclosure of yield spread premium on the GFE. Mortgage broker representatives maintained their opposition to any yield spread premium disclosure on the GFE on the grounds that disclosure would put mortgage brokers at a competitive disadvantage as compared to lenders. Mortgage brokers also stated that if brokers are required to disclose yield spread premiums, lenders should also be required to disclose par, plus pricing, and gain on sales in the secondary market. Many lender representatives at the roundtables noted that it would be difficult for a lender to disclose any profit on a loan sold in the secondary market on the GFE, since the amount could not be ascertained with any certainty in advance, but in general, they did not express support for or opposition to a requirement for broker disclosure of the yield spread premium. Some participants at the roundtables, including consumer as well as industry representatives, recommended the use of a separate mortgage broker fee agreement in lieu of the yield spread premium disclosure requirement.

The Proposed Rule. Lender payments to mortgage brokers in table funded and intermediary transactions should be clearly disclosed to consumers on the GFE, and on the HUD–1 settlement statements as set forth below. The proposed rule would also streamline the current regulatory definition of "mortgage broker."

Discussion. For the past decade, HUD has required the disclosure of YSPs on the GFE and HUD–1 documents as a "payment outside closing" or "POC." This means of disclosure proved to be of little use to consumers. Moreover, notwithstanding that lender payments to brokers are directly based on the rate of the borrower's loan, under current HUD guidance, such lender payments are not required to be included in the calculation of the broker's total charges for the transaction, nor are they clearly listed as an expense to the borrower. The confusion that can result when borrowers do not understand that mortgage brokers' total compensation includes lender payments derived from the interest rate is exacerbated by the fact that many brokers hold themselves out as shopping among various funding sources for the best loan for the borrower, while failing to explain to the borrower that the payment they receive from the lender is derived from the borrower's interest rate. On the other hand, some brokers tell their customers

[20] "YSP POC" sometimes appears on the second page of the HUD–1/1–A to represent "Yield Spread Premium Paid Outside of Closing," which is rarely understood by borrowers as a payment they make out of their above-par interest rate.

[21] 66 FR 53056.

how they can use lender payments to lower the customer's up-front settlement costs.

The 2001 Policy Statement made clear that earlier disclosure and the entry of yield spread premiums as credits to borrowers would "offer greater assurance that lender payments to mortgage brokers serve borrowers' best interests." [22] HUD could not mandate new disclosure requirements in the 2001 Policy Statement. HUD did, however, commit itself in the 2001 Policy Statement to making full use of its regulatory authority to establish clearer requirements for disclosure of mortgage broker fees, and to improve the settlement process for lenders, mortgage brokers, and consumers.[23]

It is for this reason that HUD proposed its new disclosure requirements in the July 2002 Proposed Rule. Having carefully considered the NAMB's and other comments in response to the 2002 proposal, as well as the comments presented at the RESPA Roundtables, and the results of consumer testing by the Federal Trade Commission (FTC) and HUD, as discussed below, HUD maintains that while YSPs to mortgage brokers must be clearly disclosed to borrowers, at the same time, mortgage brokers also must not be disadvantaged in the marketplace, since such disadvantage will only result in decreased competition and higher costs to consumers. Many mortgage brokers offer products that are competitive with and frequently lower priced than the products of retail lenders, as evidenced by brokers' large and growing share of the loan origination market, and HUD wishes to preserve continued competition and lower cost choices for consumers.

Today's proposed rule also streamlines the current regulatory definition of "mortgage broker." Under the proposed definition, "mortgage broker" means a person (not an employee of the lender) or entity that renders origination services in a table funded or intermediary transaction. The definition would also apply to a loan correspondent approved under 24 CFR 202.8 for FHA programs.

The proposed definition would eliminate the current exclusion of an "exclusive agent" of a lender from the definition of "mortgage broker." The current definition essentially excludes some persons who perform the same services as mortgage brokers as defined in 24 CFR 3500.2. In order to improve disclosure of settlement charges and increase transparency, HUD believes that all persons who perform mortgage broker services should be subject to the disclosure requirements. Therefore, an "exclusive agent" of a lender who is not an employee of the lender, but who renders origination services in a table funded or intermediary transaction, would be subject to the mortgage broker disclosure requirements set forth in this proposed rule.

HUD Research on Mortgage Broker Disclosures

1. *HUD's Testing of the GFE.* In October 2002, HUD contracted with a communication and consumer testing expert, Kleimann Communication Group, to revise and test the GFE and mortgage package forms,[24] in order to assure that the forms were user-friendly and enabled consumers to identify the least expensive loan. With respect to the GFE, the testing had the additional purpose of showing and explaining yield spread premiums and discount points to borrowers. New homebuyers and experienced homebuyers were part of the groups tested. The groups included members from diverse racial and ethnic groups, the elderly, and low-education and low-income groups. The testing of the GFE form was conducted in two phases.

2. *Phase 1 HUD Testing.* In Phase 1, the contractor conducted three rounds of one-on-one testing interviews to collect data about form comprehension and potential sources of confusion. The goal of the testing was to fine-tune and develop the GFE form and ensure that consumers can use the GFE in the way intended. Testing in this phase solicited consumer feedback through individual interviews with consumers as they actually used the GFEs in the simulated task of buying a home and needed to select between several loan offers. The data provide guidance about problems consumers have and the reasons for those problems. This phase consisted of three rounds of testing.

Each of the first two rounds of testing involved interviews with a total of 45 consumers in three cities. The contractor made several format and language changes to the form, as it was published in the July 2002, proposed rule, to improve readability and clarity. Among other changes, a summary page was developed and tested, with the specific charges for individual categories of settlement services appearing on a second page of the form. Kleimann then developed a comprehensive testing protocol that addressed the key objectives of the GFE form for consumers. The interviews with each participant lasted for 90 minutes with a 10-minute break. The interviews had two parts, one unstructured and one structured. In the unstructured portion of the interview, participants were asked to think aloud as they looked at each form for the first time. This unstructured and unprompted portion of the interview allowed Kleimann to capture users' initial reactions, including to areas that they responded well, to areas they did not understand, and to areas they questioned. The unstructured portion also ensured that the testers did not influence the comments of the participants by leading them to discuss information they would not have noticed on their own.

In the structured portion of the interview, Kleimann gave each consumer completed GFEs (as well as MPOs) and asked targeted questions to determine how well participants understood certain areas of the forms, whether the consumers could determine the least expensive loan, and how the forms might be improved. The study design focused on how the forms performed as stand-alone documents. The interviewer neither helped the participant understand any of the information on the forms nor answered any questions the participant asked to clarify information.

In these tests, 90 percent of participants chose the least expensive loan, when confronted with a choice between a GFE representing a loan from a lender (with no YSP shown) and a GFE representing a loan from a broker (with the YSP disclosed). The percentage increased slightly to 93 percent when an MPO was included as a third option.

Participants also understood the forms well. They could identify the basic loan costs and loan features. Over 90 percent could identify the total estimated settlement charges. The tested forms retained the trade-off table shown on the forms in the 2002 Proposed Rule, showing borrowers that if they wanted to receive a lower interest rate, they would have to pay more at settlement, and vice versa; 90 percent understood the trade-off table. About two-thirds of the participants could distinguish between items they, as consumers, could shop for and items for which they would use the broker's or lender's

[22] 66 FR 53056.

[23] 66 FR 53053.

[24] As noted in Section III above (Overview of HUD's Efforts Since 2002), the 2002 Proposed Rule included a "guaranteed mortgage package agreement" or "GMPA," and HUD's contractor initially tested both the GFE and GMPA forms. In subsequent rounds of testing, the name of the GMPA form was changed to "mortgage package offer" or "MPO" and is referred to in this document as "MPO."

providers; almost two-thirds could explain the adjusted origination charge; and 70 percent of participants were able to identify the tolerances correctly in round 2 testing.

During the testing, Kleimann asked participants a number of questions about how they felt about the forms—how comfortable or uncomfortable they felt with the forms, what they liked and disliked, and how they perceived the information and the level of writing. Participants reacted very positively to the GFE layout and language, and to the clear delineation of charges. They found the summary page on page 1, the breakdown of charges on page 2, and the trade-off table on page 3 to be particularly useful. In round 2 of testing, 86 percent said the GFE had the right information for them, almost 90 percent said the GFE was written at the right level for them, and about two-thirds of participants said they were comfortable with the forms.

This testing was designed to see how the GFE form would perform as a stand-alone document. The interviewer neither coached nor led the participant by asking questions before the participant could work alone with the document. While this technique identifies how well participants use the GFE form as a stand-alone in a testing situation, consumers using these forms in the context of actual situations may perform even better. First, this testing involved no interaction at all between the potential borrower and a loan originator. In an actual situation, a loan originator would be able to answer borrower questions about the information on the forms and improve the borrower's understanding of it. Of course, some originators might try to confuse the borrower in order to collect higher fees, but a competitor might be more than willing to clear up that confusion, since doing so might get him the borrower's business. In addition to the help coming from the originator, borrowers could always ask someone else for help: A spouse, friend, their real estate agent, etc. Moreover, local consumer groups that focus on lending issues will also assist borrowers in understanding the new, streamlined GFE form. Since none of these sources were available during the testing, the Kleimann results should be viewed as underestimates of how much the new forms will help consumers once the forms are placed in an actual context of obtaining financing to purchase a home or refinance an existing loan. The third round of testing consisted of 60 participants, with 15 each in four cities, following the same procedures as in the first two rounds of testing.[25] The GFE form was changed in order to consider whether an alternative presentation of the discount points and yield spread premium, suggested by the National Association of Mortgage Brokers, would increase consumer understanding. The yield spread premium (YSP) and discount point disclosure was removed from the top of page 2, where it had been integrated into the calculation of total up-front charges to the borrower, and moved to page 3. As a consequence, page 2 included only the adjusted origination charge at the top. Thus, otherwise identical loans from a broker and a lender would have identical figures on page 2 as well as on page 1 of the summary. Page 3 contained the YSP and discount points. The form did not include a full calculation of total broker compensation, and thus differed from both the proposed rule and the first two rounds of testing.

The results showed that participants could continue to identify the cheapest loan: 93 percent of the participants correctly selected the broker loan as the cheaper loan as opposed to 90 percent in round 2. Also, in round 3 of testing, 89 percent of participants would have chosen the cheaper broker loan as opposed to 86 percent in round 2. None of the differences between these percentages in round 2 and round 3 is statistically significant. Also, as in the first two rounds, participants generally liked the form and would use it to comparison shop. They could identify the basic terms of the mortgage and the estimate of total settlement costs, and 86 percent understood the trade-off table. The material seemed to be presented at the right level and to be clearly laid out. Participants again identified the summary page, the breakdown of charges, and the trade-off table as useful.

However, participants had trouble understanding the concepts of YSP and discount points.[26] Only 3 percent and 30 percent, respectively, of the participants could paraphrase what YSPs and discount points represented, leaving over two-thirds of the participants unable to paraphrase. Participants did not understand how these two concepts (now located on page 3) related to other settlement charges (on page 2). Essentially, placing these terms outside the calculation of origination charges (that is, on page 3 instead of page 2 as in the first two testing rounds) seems to decrease participants' understanding of how the YSP and discount points fit into total loan costs. Since there was no significant improvement in participants' ability to determine the cheapest loan, and most participants did not understand the concept of YSP, HUD decided to keep the YSP on page 2 in the calculation in the 2005 Proposed Rule, as was the case in the 2002 Proposed Rule.

3. *FTC Testing.* During the same period that HUD was developing the revised GFE, FTC tested the effect of YSP disclosure to see if the disclosure had an adverse effect on the consumer's ability to comparison shop. Using a variation on the GFE form tested by Kleimann in round 2 testing, FTC extracted and tested a portion of the form. The first page of the extract consisted of an abbreviated version of the Summary Table from page 1 of the GFE. The second page of the extract contained the "Your Charges for Loan Origination" box and an abbreviated version of the "Your Charges for All Other Settlement Services" box from page 2 of the GFE. As a control, FTC took these same two extracts and eliminated the YSP and service charge, producing a second set of extracts. Thus, FTC isolated elements of the proposed GFE and created two variations of their extracts: with the YSP and without the YSP. FTC also tested the YSP disclosure from the GFE in HUD's 2002 Proposed Rule, and an alternative disclosure using language developed by FTC to describe the YSP and other loan terms.

FTC testers gave each participant a pair of loan extracts to evaluate: one had no YSP and thus represented a lender loan, and the other contained a YSP and thus represented a broker loan. The broker loan was $300 less than the lender loan. FTC asked participants which loan was cheaper and also which loan the participant would choose. Each participant also received a second set of extracts in which each loan offer was the same cost. The participants were asked the same two questions: which loan was cheaper and which loan would the participant choose.

FTC tested five groups with 103 or 104 participants per group. The results using the GFE variation of HUD's second round of testing are most relevant to the 2005 Proposed Rule. When the YSP was disclosed and the broker loan offer was cheaper, 72 percent of participants could correctly identify the broker loan as the cheaper loan; 17 percent incorrectly identified the lender loan as cheaper. Asked to identify which loan offer they would choose, 70 percent of participants

[25] The cities were Wilmington (Delaware), Tulsa, Minneapolis, and Los Angeles.

[26] These results are consistent with the work of Jackson and Berry (2001) and Woodward (2003a).

would have chosen the cheaper broker loan; and 16 percent would have chosen the lender loan. In contrast, when the form extract did not disclose the YSP, 90 percent correctly identified the broker loan as cheaper, and 85 percent would have chosen it. Disclosing the YSP caused an 18 percent drop in participants correctly identifying the cheaper loan and a 14 percent drop in the number who would choose it in the market. When costs of the broker and lender loans were the same on GFE forms that contained the YSP, participant performance decreased. Fifty-three percent reported that the loan costs were a tie; 30 percent believed the lender was cheaper; 11 percent believed the broker was cheaper. When asked to identify which loan offer they would choose, 25 percent of the participants chose either the lender or the broker loan offers; 46 percent selected the lender loan offer; and 17 percent selected the broker offer. In contrast, when the form omitted the YSP, 96 percent correctly identified the tie, and 78 percent chose one or the other as their preference.

FTC concluded that the YSP disclosure on the GFE form extract it tested had two drawbacks. First, its YSP disclosure impaired the ability of borrowers to comparison shop leading many to choose the more costly alternative. Second, the YSP disclosure introduced bias in the selection process that favored lenders over brokers. The Department's goal is to promote consumer shopping for mortgages and to prevent bias against any loan originator.

4. *Phase 2 HUD Testing.* FTC conducted its tests in February and March of 2003, and briefed HUD on the results during the summer of 2003. HUD decided to undertake additional testing and to incorporate the FTC test results in the further testing. For round 4 of testing, HUD asked Kleimann Communication Group to parallel aspects of the FTC study, including the questions asked, the difference between the amounts of each offer, and the length of the test situation.[27] HUD continued to test a full-length GFE rather than the portion tested by FTC, because HUD thought that the context of the entire form might provide a more accurate measure of participants' understanding of the GFE.

For round 4 of testing, 600 participants were selected; all received full GFEs. The control group received GFEs that omitted the YSP disclosure, while the experimental group received GFEs with the YSP disclosed. Each participant was given two pairs of loans: one in which the broker loan was $300 less than the lender and one in which the broker and lender loan offers were the same cost. Each participant was asked three questions for each set of GFEs: (1) Which offer was cheaper or if they cost the same, (2) which offer would they choose, and (3) why they made that choice. The results of this testing showed both consistency with and divergence from the FTC results.

When the YSP was disclosed, 83 percent of the participants correctly identified the broker loan as cheaper, and 8 percent incorrectly identified the lender as cheaper. These results were an improvement over the FTC results of 72 percent and 17 percent. In this GFE scenario, 72 percent of the participants said they would choose the broker offer and 11 percent said they would choose the lender. Similarly, in the FTC study, 70 percent of the participants chose the broker offer and 16 percent chose the lender offer.

When the YSP disclosure was removed, 92 percent correctly identified the broker loan as cheaper, and 1 percent incorrectly identified the lender as cheaper. These results are quite similar to FTC's results of 90 percent and 4 percent. When asked to choose a loan, 88 percent of participants chose the broker offer, while 1 percent chose the lender loan. These results compare to 85 percent and 3 percent respectively in the FTC testing.

When given same cost loan offers with a YSP, 81 percent correctly identified both loans as costing the same; 15 percent incorrectly identified the lender as cheaper; and 3 percent incorrectly identified the broker as cheaper. In contrast, in the FTC study, only 53 percent correctly identified the offers as costing the same; 30 percent incorrectly identified the lender as cheaper; and 11 percent incorrectly identified the broker as cheaper. In this GFE scenario, 50 percent of participants would have chosen either offer; 39 percent chose the lender offer; and only 5 percent chose the broker's. In contrast in the FTC study, only 25 percent chose either offer; 46 percent chose the lender offer; and 17 percent chose the broker's offer.

Of particular concern was the difference between participants who could identify the cheapest loan offer, but did not choose it. Analysis of the participant responses to the open-ended question of "why did you choose that offer" led to further modifications of the GFE to address this concern and to a fifth round of testing. In many comments, participants stated that they chose a particular offer because they did not want the "higher interest rate" indicated on page 2 of the GFE. They concluded from the language on the YSP disclosure that the interest rate was higher than the rate cited on page 1 under "Loan Details." Also, many of those who had no preference for the cheaper broker loan indicated that $300 was not a sufficient difference to be a deciding factor.

As a result of the testing and analysis, revisions were made to the GFE. First, the language in box 2 on page 2 of the GFE referring to the "higher interest rate" and "lower interest rate" was modified to reduce the possibility of borrowers" misinterpreting that the interest rate had changed from what was reported on the first page. Second, a third option was added to the YSP/discount points section on page 2 so a lender could indicate that its credits or charges were already included in "Our Service Charge." This addition was designed to ensure that participants would understand that a lender's origination charge might include a YSP or discount points, even though the YSP or points would not necessarily be known at the time of settlement, because the loan would not have been sold into the secondary market. The third option thus creates a closer parallel between broker and lender loans. Third, arrows were added on pages 1 and 2 to focus the borrower's attention on the subtotals and the total estimated charges, rather than on individual components. In addition, the typeface point size in the Total Estimated Settlement Charges on the bottom of page 1 was increased to further draw attention to the bottom-line.

For purposes of testing, three other changes were made to the GFEs. First, the difference in the total cost was changed to $500, to increase the likelihood that the difference would be a deciding factor. Second, another pair of loan options was added in which the lender offer was $500 less than the broker offer. This addition was intended to identify any bias for or against the broker and lender options. Finally, a set of four loans was added, to investigate whether the comparison across more than two offers increased or decreased participant performance. No version was tested without the YSP and discount points language.

[27] Kleimann's report, entitled *Consumer Testing Results for HUD's Good Faith Estimate (GFE) Form: Rounds 4 & 5* (dated March 19, 2004), provides information on the specific characteristics of the consumers tested, revisions that Kleimann made to the form and the reasons for those revisions, the specific cities where the tests were conducted, the testing protocols, testing conditions, and the main results from each round of testing.

For round 5 of testing, 600 participants were divided into two groups, both of which received the revised GFE.[28] The first group received the revised GFE with changed language and with the addition of a third option so that lenders could indicate that YSP and discount points had been included in "Our Service Charge." The second group received the identical revised GFE, but the third option box was removed. All participants received three pairs of loans, one with the broker offer being lower by $500, one with the lender offer being lower by $500, and one in which both offers were the same. In addition, each participant received a set of four offers to compare.

The three option GFE and the two option GFE performed quite similarly with the three option form consistently getting slightly better results. The proposed rule therefore discusses only the three option form, and that form is included in the proposed rule.

In the GFE in which the broker was cheaper, 92 percent of the participants correctly identified the broker as the cheaper loan offer. This result represents an improvement over the 72 percent reported by the FTC study and the 83 percent reported in the round 4 results. Only 3 percent of the participants incorrectly identified the lender as the cheaper loan offer, compared to the 17 percent reported by the FTC and 8 percent in round 4. When asked to choose a loan, 87 percent of the participants chose the cheaper broker loan as compared to 70 percent of the participants in the FTC study and 72 percent of the participants in round 4. These results of round 5 of testing are significantly better than the FTC's results and are based on a much larger sample.

In the GFE in which the lender was cheaper, 92 percent of the participants correctly identified the lender as the cheaper loan offer. Only 1 percent incorrectly identified the broker as cheaper. When asked to choose a loan, 89 percent of the participants chose the lender loan and less than 1 percent chose the broker.

The purpose of testing the case in which the lender was cheaper than the broker was to test for bias by seeing if the GFE forms performed equally well when either the lender or broker was the cheaper loan. A comparison of the results indicates that there is no bias against brokers when the loans have different borrower costs.

In the GFE in which the broker and lender loan offers were of equal cost, 90 percent of the participants were able to correctly identify that fact. This result compares very favorably with the 53 percent reported by FTC and the 81 percent from round 4 of testing. Participants in round 5 misidentified the lender as cheaper seven percent of the time, compared to 30 percent in the FTC results and 15 percent in round four. Participants misidentified the broker as cheaper 1 percent of the time as compared to 11 percent in the FTC study and 3 percent in round 4. Participants said they would choose either loan 70 percent of the time, a dramatic increase over the 25 percent in the FTC study and the 50 percent in round four. Twenty-one percent would choose the lender as compared to 46 percent in the FTC study and 40 percent in round 4. Four percent of participants chose the broker compared to 17 percent in the FTC study and 5 percent in round 4 of testing.

To further test whether increased context improved or decreased consumer performance with the revised GFE, the Department asked Kleimann to give the participants a four-loan comparison as well. For this four-way comparison, HUD included a blank worksheet or shopping chart to aid participants in comparing the loans, as page 4 of the GFE form. The worksheet contained spaces for the originator's name, loan amount, interest rate, term, monthly payment, adjusted origination charge, charges for all other settlement services, and total estimated settlement charges. On page 1 of the GFE, a sentence telling participants to use the table to compare offers was inserted. Additionally, half of the participants were given explicit verbal directions to use the worksheet.

The 300 participants who had received the three option GFE were included in this four-way comparison. Half were given a set in which a broker loan offer was the cheapest. The other half were given a set in which a lender and a broker loan offer cost exactly the same and were the cheapest at $6,500. Only 150 participants received explicit verbal instructions to use the worksheet in their comparison, while half received no instructions.

In the comparison in which a broker loan offer was the cheapest, 92 percent of participants who were not verbally reminded to use the comparison worksheet correctly reported the broker loan as the cheapest. Very few of the participants who were not verbally reminded to use the comparison worksheet used it. When instructed to use the comparison sheet, many participants did, and 97 percent correctly identified the broker loan as the cheapest. The overall success rate for correctly identifying the correct loan as the cheapest for both those getting and those not getting the verbal instructions to use the comparison worksheet was 95 percent, with only 1 percent misidentifying a lender loan as cheaper.

In the case where both loans cost the same and no verbal instructions were given to use the comparison sheet, 41 percent picked the broker loan as cheaper and 49 percent picked the lender loan. With verbal instructions to use the worksheet, 57 percent picked the broker at $6,500 and 35 percent picked the lender at $6,500. The combined average was 49 percent for the broker and 41 percent for the lender. There was no bias against the broker when costs were the same.

5. *Sixth Round of Testing.* HUD conducted a sixth round of consumer testing in November 2007. The testing consisted primarily of qualitative tests of the GFE and an introductory qualitative test of the closing script (referred to in testing as "the summary"). Compared to previous rounds of testing, the testers found that participants were more aware, due to recent intensive media coverage of mortgage market difficulties, personal experience, and the experiences of relatives and friends, of the issues facing a consumer choosing a mortgage loan. The modifications to the GFE for round 6 included an expanded disclosure of loan terms on page 1 of the GFE, clarifying language regarding the important dates when actions must be taken by the consumer, changes in the title and description of government recording and transfer charges, and new language regarding additional compensation lenders may receive after closing for selling the loan.

Consumers appreciated the enhanced loan terms disclosures designed to alert the borrower to potentially unfavorable changes in their obligations during the term of their loans. Participants stated that they liked the form length, the language of the GFE, and the layout of pages 1 and 2. Participants appreciated the trade-off table on page 3 and used it to compare loans. As a result of the round six testing, information on the existence of an escrow account was added in the "Summary of your loan terms" section on page 1, and a section entitled "Your financial responsibilities as a homeowner" was added at the top of page 4. Finally, the tolerance presentation was changed from a pure list of headings and bullets on page 3,

[28] Participants were chosen for demographic diversity in the same five cities: Atlanta, Boston, Denver, Seattle, and Tulsa. No participant from round 4 was permitted to participate in round 5.

to bullets within columns according to the tolerance that applies.

Testers conducted settlement/closing simulations to test the idea of the closing script. Participants thought the loan details were clear and understandable and reacted positively to having the summary read aloud. Participants were more attentive to loan details, were more aware of the tolerance categories and how they related to charges, and were better able to identify tolerance violations when the script was read aloud than when they reviewed the script documents independently.

Revisions to the GFE Based on Testing

The GFE form proposed today is the result of an iterative testing process comprised of six rounds of consumer testing of the form during the 2003–2007 period. HUD's testing contractor used the data collected from testing participants during each round to improve and modify the form throughout the testing process. A summary report with detailed information on each round of testing is available at *http://www.huduser.org/publications/hsgfin/GoodFaith.html*. Based on this testing, HUD has made revisions in the GFE disclosure form and now presents the net origination charge on the first page of the form as "your adjusted origination charges." This amount is added to the charges for all other services to arrive at the total estimated settlement charges for the mortgage on the first page. This new approach to disclosure helps consumers focus appropriately on the net charges of the originator when comparing similar loans, from either a lender or a broker, and on the total estimated settlement charges. The fourth page of the form provides a Mortgage Shopping Chart that also helps borrowers compare total charges for various mortgage loans.

The second page of the new GFE informs the consumer how the adjusted origination charge is computed. Block 1 discloses as "Our service charge" the originator's total charge to the borrower for the loan. (The form no longer refers to this total charge in Block 1 as "maximum" compensation.)

Today's proposed rule proposes to require that in the case of loans originated by mortgage brokers, the amount in Block 1 must include all charges received by the broker and any other originator for, or as a result of, the mortgage loan origination, including any payments from the lender to the broker for the origination. In the case of loans originated by originators other than mortgage brokers, the amount in Block 1 must include all charges to be paid by the borrower that are to be received by the originator for, or as a result of, the loan origination to the borrower, except any amounts denominated by the lender as discount points or amounts that the lender chooses to call a credit and which are disclosed in Block 2.

Block 2 discloses for loans originated by mortgage brokers whether there is any charge or a credit to the borrower for the specific interest rate chosen for the GFE. The second check box indicates whether there is a payment for a higher interest rate loan described, as the "credit of $____ for this interest rate of __%. This credit reduces your upfront charges." The third check box indicates any "charge of $____ for the interest rate of __%. This payment (discount points) increases your upfront charges." Any lender payment is then subtracted and any points are added to arrive at "your adjusted origination charge" that is also disclosed on the first page of the form. For mortgage brokers, the amounts of any charge or credit in Block 2 must equal the difference between the price the wholesale lender pays the broker for the loan and the initial loan amount.

At page 2, while lenders are not required to check the second or third boxes of Block 2, in loans where they do not make such disclosures, they are required to check box 1 that indicates that "The credit or charge for the interest rate chosen is included in the service charge." If lenders denominate any amounts due from the borrower as "discount points," they must check the third box indicating that there are charges for the interest rate and enter the appropriate amount for points as a positive number. If lenders denominate any amounts as a credit to the borrower for the particular interest rate covered by the GFE, they must check the second box and enter the appropriate amount as a negative number. Lenders must also add any such positive amounts or deduct any negative amounts to arrive at "Your Adjusted Origination Charge," which is also to be disclosed on page 1 of the form.

Considering that mortgage brokers are required to disclose payments from lenders while lenders are not required to disclose payments they receive from the secondary market, by virtue of the "secondary market exemption,"[29] HUD considered providing only the adjusted origination charge and disclosing the YSP and discount points elsewhere on the form without the calculation. HUD concluded, however, that a complete disclosure of payments to the broker as presented on page 2 of the form, read in conjunction with the chart on page 3 of the form, was essential to borrower understanding of: (1) The broker's total compensation; (2) how rate-based payments from lenders can help reduce borrowers' up-front origination charges and settlement costs in brokered loans; and (3) how payments to reduce the interest rate and monthly payment increase up-front charges. Because mortgage broker compensation occurs at settlement and can be readily ascertained, full disclosure of total broker compensation is appropriate. On the other hand, even in the absence of the secondary market exemption, a similar disclosure of lender compensation would not be appropriate because it is difficult to measure secondary market payments with any precision at the time of settlement and because a lender may or may not choose to sell a particular loan at some point in the future. However, the GFE form includes a notation on page 4 that lenders may also receive an additional payment if they sell the loan after settlement.

Furthermore, based on testing by HUD's contractor, as discussed above, the YSP disclosure without an explanation of its context was not useful to consumers. On the other hand, based on testing, by moving to a form that requires in Block 2 that lenders disclose that credits or charges may be included in their service charge as well, even when the calculation is on the form for brokered loans, borrowers are not confused and correctly compare adjusted origination charges between loans from mortgage brokers and loans from lenders even when the YSP is included in the calculation of the adjusted origination charge. Nevertheless, to help borrowers identify the lowest-cost loan without being confused by the presence of a YSP, HUD established the first page of the form as a summary page that only includes adjusted origination charges, moved the "calculation" of any credit (YSP) or charge to the second page of the new GFE, and then established the new Mortgage Shopping Chart at page 4 to facilitate comparison shopping. HUD is now convinced that by making these changes, any disadvantage to brokers is virtually eliminated. Also, consistent with the FTC's 2002 comment, HUD proposes to include in the revised Special Information Booklet advice to borrowers that lenders also may receive payments from financial institutions when they sell the mortgage but are not

[29] As set forth in 24 CFR 3500.5(b)(7), a bona fide transfer of a loan obligation in the secondary market is not covered by RESPA and this part, except as set forth in section 6 of RESPA (12 U.S.C. 2605) and 24 CFR 3500.21.

required to disclose such payments and, for this reason, borrowers should focus on net origination charges of loan originators for comparable mortgages.

To avoid borrower confusion, the term "lender payment to the borrower" that had been included in the 2002 Proposed Rule also has been dropped. Through its use of this term in the earlier proposal, HUD had sought to have borrowers focus on the payment, and understand that it was a consequence of their choice of rate. HUD now recognizes the original terminology warranted improvement.

In arriving at changes in the proposed revised GFE form, HUD also considered the possibility of adopting the Mortgage Broker Fee Agreement developed by representatives of the lending and brokerage industries. These forms disclose the total amount of fees to the broker and explain that the fees may include lender payments, but not the specific amount of such payments. HUD believes, however, that it is better for the borrower to understand the lender payment and its relationship to higher interest rates so that he or she can use the payment to lower his or her up-front costs, rather than simply to disclose the possibility of such payment to the borrower. For these reasons, HUD remains committed to improving the GFE disclosure rather than requiring yet another new form or agreement.

In its consultations with staff of the Federal Reserve, HUD raised the concern expressed by some commenters that treating lender payments to mortgage brokers as a credit toward the origination charges could increase the points and fees of each brokered mortgage loan, resulting in more loans coming under HOEPA coverage. Federal Reserve staff advised HUD that, notwithstanding HUD's changed requirements, determinations of whether payments to a mortgage broker must be included in the finance charge and whether a loan is covered by HOEPA are based on the statutory definitions and requirements in TILA as implemented by the Board's Regulation Z, which are unaffected by HUD's RESPA rulemaking.

HUD also recognizes that many loan originators today offer loans with no up-front fees due from the borrower. These loans have become more popular over the years. The proposed GFE can easily accommodate these "no cost" loans. In the case where "no cost" means no up-front payment to the loan originator, the figure in Block A equals zero. This implies that any credit identified in Block 2 would exactly offset the charge in Block 1. While a mortgage broker would always be required to enter the actual amount of any yield spread premium in Block 2, a lender could alternatively enter zero for the credit, in which case the charge in Block 1 would also have to equal zero so that the combination to be reported in Block A would equal zero.

Alternatively, the borrower might want to pay a lower interest rate and monthly payment than that associated with a "no cost" loan. The borrower generally may do this by buying the interest rate down. This is done by paying an up-front fee to the loan originator that compensates the loan originator for the lower interest rate and monthly payments it will receive over the life of the loan. The more the borrower pays, the lower the interest rate and monthly payments will be. The amount the borrower pays to buy the rate down shows up in Block A as a positive number. This would result from a higher value in Block 1 or a higher value in Block 2. (A lower credit in Block 2 or a higher charge in Block 2 yields a higher value in Block 2, and in Block A as well.) Thus, either "no cost" loans or those where the borrower buys down the interest rate can be accommodated on the proposed GFE. In the first case, the value in Block A is zero. In the second, Block A represents what is paid to buy the interest rate down.

In the case where "no cost" encompasses some third party fees as well as the up-front payment to the loan originator, the figure in Block A would have to be a negative value large enough to offset the third party fees covered under this definition of "no cost." For brokers, who are required to report yield spread premiums, this implies that the yield spread premium identified in Block 2 as a credit would be larger than the charge in Block 1. The sum of the positive value in Block 1 and the negative value, the credit, in Block 2 would equal a negative value large enough to offset the third party fees. Lenders are not required to report yield spread premiums. But they are permitted to enter credits in Block 2. If a lender chooses to do so, then the yield spread premium identified in Block 2 as a credit would have to be larger than the charge in Block 1. Just as in the broker case, the sum of the two would equal a negative value large enough to offset the third party fees for a "no cost" loan. Finally, today's proposed rule states that loan originators must include all charges correctly within their prescribed category on the GFE and the HUD–1 (or HUD–1A). The amounts for categories involving third parties can include only amounts paid to the third party, and must not include amounts retained by the loan originator for related services performed by the loan originator. The amount charged to the borrower and shown on the HUD–1 in an individual transaction may be based on an average calculated in accordance with proposed § 3500.8(b)(2). (See Section E discussion on average cost pricing.) HUD believes these rules are required to assure that, pursuant to Sections 4 and 5 of RESPA, originators provide borrowers accurate disclosures of settlement charges on the GFE, HUD–1, and HUD–1A.

FHA Limit. Under its current regulations, HUD places specific limits on the amount a mortgagee may collect from a mortgagor to compensate a mortgagee for expenses incurred in originating and closing a FHA-insured mortgage loan (see 24 CFR 203.27).[30] In light of the considerations below and its proposed changes to the HUD–1/1A, HUD is today proposing a change to the FHA regulations limiting origination fees of mortgagees. FHA considered deregulating the loan origination fee limitation in 1988 (see 53 FR 15408, April 28, 1988), but did not pursue a final rule at that time.

HUD believes that its RESPA policy statements on lender payments to mortgage brokers restrict the total origination charges for mortgages, including FHA mortgages, to reasonable compensation for goods, facilities, or services.[31] While the FHA limit on origination fees only regulates fees from mortgagors to mortgagees and does not include any payments between mortgagees, HUD is aware that in recent years mortgage brokers have routinely utilized yield spread premiums in FHA mortgage transactions to supplement their compensation beyond the amount they receive directly from the borrower. Studies by HUD confirm this.

HUD believes that improvements to the disclosure requirements for all loans sought to be achieved as a result of the rulemaking should make total loan charges more transparent and allow market forces to lower these charges for all borrowers, including FHA borrowers. Therefore, HUD is proposing in this

[30] Under 24 CFR 203.27(a)(2)(i), origination fees are limited to one percent of the mortgage amount. For new construction involving construction advances, that charge may be increased to a maximum of 2.5 percent of the original principal amount of the mortgage to compensate the mortgagee for necessary inspections and administrative costs connected with making construction advances. For mortgages on properties requiring repair or rehabilitation, mortgagor charges may be assessed at a maximum of 2.5 percent of the mortgage attributable to the repair or rehabilitation, plus one percent on the balance of the mortgage. (See 24 CFR 203.27(a)(2)(ii) and (iii).)

[31] See Statement of Policy 1999–1, 64 FR 10080, March 1, 1999, and Statement of Policy 2001–1, 66 FR 53052, October 18, 2001.

rulemaking to remove the current specific limitations on the amounts mortgagees presently are allowed to charge borrowers directly for originating and closing an FHA loan. The FHA Commissioner would retain authority to set limits on the amount of any fees that mortgagees charge borrowers directly for obtaining an FHA loan.

The proposed rule would also permit other government program charges to be disclosed on the blank lines in Section 800 of the HUD–1/1A.

G. Modification of the HUD–1 Settlement Statement

The Proposed Rule. The current HUD–1/1A Settlement Statements would be modified to allow the borrower to easily compare specific charges at closing with the estimated charges listed on the GFE. In addition, an addendum would be added to the HUD–1/1A that would compare the loan terms and settlement charges estimated on the GFE to the final charges on the HUD–1 and would describe in detail the loan terms for the specific mortgage loan and related settlement information. The settlement agent would be required to read the addendum aloud to the borrower at settlement and provide a copy of it at settlement.

Discussion. As recommended at the 2005 RESPA Roundtables, HUD is today proposing to modify the HUD–1/1A form to make it comparable to the GFE. The HUD–1 is well accepted as a listing of settlement service charges by industry and consumers alike. However, there is a risk that if a borrower cannot easily compare the estimated charges listed on the GFE with the settlement charges listed on the HUD–1/1A, a settlement service provider could deviate from the prices listed on the GFE and the borrower would not realize such deviation prior to closing. Thus, borrowers would not be able to fully realize the financial savings that will result from comprehensive RESPA reform. Many participants at the RESPA Reform Roundtables recommended that in order to ensure the maximum cost savings to borrowers, the GFE and the HUD–1 should be easily comparable so that borrowers will be able to compare the estimated costs with the actual costs at closing. While some participants recommended that a new GFE be designed to correspond to the HUD–1, others recommended that the HUD–1 be redesigned to correspond to a new GFE that includes major cost categories.

HUD recognizes that the HUD–1/1A forms are the most widely used and accepted forms in the mortgage industry and does not undertake changes to these forms lightly. However, because HUD believes that the GFE and the HUD–1 should be easily comparable, today's proposal sets forth changes to the HUD–1/1A that will allow borrowers to easily compare the figures on the GFE to the final charges at settlement. The proposed changes facilitate comparison of the two documents by inserting, on the relevant lines of the HUD–1/1A, a reference to the corresponding block on the GFE. With such changes, a borrower would be able to easily compare a figure in a particular column on the HUD–1/1A with the corresponding figure on the GFE. In addition, creating new labels for lines, showing totals while still permitting disclosure of details so long as not shown in either column or paid outside closing (POC), and leaving blank lines allows the HUD–1 to still function as an effective settlement document.

The instructions for completing the HUD–1 will clarify the extent to which charges for individual services must be itemized. In general, the HUD–1 must separately itemize every service provided by a third party (i.e., other than the loan originator) to show the name of the party ultimately receiving the payment, along with the total amount received. However, services connected to the origination of the loan must not be separately itemized, even if a loan originator uses a third party to perform those services. For example, charges for document handling or processing should not be separately itemized, but instead should be included in the loan originator's own charge, since those types of services are ordinarily performed by the loan originator itself. Today's proposed rule adds a definition of "origination services" to clarify the types of services that may not be separately itemized on the HUD–1.

The instructions for completing the HUD–1 also clarify the extent to which charges for title services must be itemized. In general, the HUD–1 must separately identify each service provider that is performing title services, along with the total amount received. If a party other than the title company listed on line 1101 of the HUD–1 provides services that are separate from providing title insurance, such as attorney and settlement or escrow agent services, the title company should separately itemize those services with the total amount paid to that provider, to the left of the columns. However, charges for services defined as "primary title services" such as abstract, binder, copying, document handling, or notary fees, should not be separately itemized on the HUD–1, even if a party other than the title company listed on line 1101 of the HUD–1 provides those services.

Today's proposed GFE distinguishes between those settlement costs attributable to the loan originator and charges for all other settlement services. However, Section 800 of the current HUD–1/1A forms combines loan originator costs and some third party costs under the same heading ("Items Payable in Connection with Loan"). In order to facilitate comparison between the GFE and the HUD–1/1A for this section, the proposed HUD–1 replaces the existing line descriptions on the current HUD–1/1A with the relevant headings from the GFE. Thus, Line 801 on the proposed HUD–1 lists "Our service charge (from GFE #1)" to refer back to Block 1 on the GFE. In lieu of the "Loan discount" terminology on the current Line 802 of the HUD–1/1A, the proposed Line 802 includes "Your charge or credit for the specific interest rate chosen (from GFE #2)" to refer back to Block 2 on the GFE. Line 803 of the proposed HUD–1/1A lists "Your Adjusted Origination Charges (from GFE Block A)" and corresponds to GFE Block A. Lines 804 to 807 on the proposed HUD–1/1A for appraisal fee, credit report, tax service, and flood certification include notations indicating that the charges are listed in Block 3 on the GFE (required services selected by the loan originator). The dollar value showing up in GFE Block A can show up as POC, in the borrower's column, or in the seller's column. On line 803, the sum of the figures labeled as POC, in the borrower's column and in the seller's column should be compared to the figure in GFE Block A. The figures on Blocks 1 and 2 of the GFE must not show up in either column or as POC in order to avoid double-counting.

For Section 900, "Items Required by Lender to be Paid in Advance," Line 901 of the proposed HUD–1/1A lists "Daily Interest Charges (from GFE #8)"; Line 902 lists "Mortgage insurance premium (from GFE #3 or #5);" and Line 903 lists "Homeowner's insurance (from GFE #9)."

For Section 1000, "Reserves Deposited with Lender," the proposed HUD–1/1A inserts Line 1001 "Reserves or escrow (from GFE #7)" and then renumbers the current lines. For Section 1100, "Title Charges," the proposed form inserts Line 1101 "Title services and lender's title insurance (from GFE #4)" and then renumbers the current lines. Line 1110 lists "Optional owner's title insurance (from GFE #10)."

For Section 1200 "Government Recording and Transfer Charges," the proposed HUD–1/1A inserts Line 1201, "Government Recording and Transfer Charges (from GFE #6)" and renumbers

current lines. For Section 1300 "Additional Settlement Charges," Line 1301 includes "Survey (from GFE #5)"and Line 1302 "Pest inspection (from GFE #5)."

The figures from Blocks 3 and 5 on the GFE are broken out and listed individually on the HUD–1 in the columns or as POC. The totals are not listed as POC or in the columns to avoid double-counting.

All items on the HUD–1/1A that correspond to an item on the GFE are made to stand out by using a different font from the other text on the HUD–1, such as by bolding the text or using italics, so it is easier for the borrower to find these numbers when comparing the forms.

Addendum to the HUD–1/1A, "Closing Script." In addition to the proposed changes to the HUD–1/1A discussed above, HUD is proposing an addendum to the HUD–1 that would be provided to the borrower at closing. The loan originator would transmit to the settlement agent all information necessary to complete the prescribed addendum to the HUD–1/1A settlement form, referred to as the "closing script." The addendum would be prepared by the settlement agent and would have to accurately reflect the loan documents and related settlement information provided by the lender. The settlement agent would be required to read the addendum aloud to the borrower at settlement. The addendum would compare the loan terms and settlement charges estimated on the GFE with those on the HUD–1 and would describe in detail the loan terms for the specific mortgage loan as stated in the mortgage note, and related settlement information. The length of the addendum would vary depending on the specifics of the borrower's loan.

HUD is proposing the addendum to address the frequent complaints it receives from borrowers that the costs quoted at the GFE stage varied considerably from the costs imposed at settlement. In addition, HUD continues to receive complaints from borrowers indicating that they were unaware or unsure of the terms of the loan provided at settlement. HUD believes that by making borrowers aware of their loan terms at the settlement, many problems after settlement can be avoided.

HUD believes that greater borrower awareness and understanding of the settlement charges will help prevent the imposition of charges at settlement that were not included at the GFE stage. By reviewing each charge with the borrower at settlement, the closing agent will be able to highlight those charges that may have changed between the GFE stage and the settlement. In this fashion, the borrower will be able to more easily question any charges at the settlement, rather than after the settlement, when it becomes more difficult to address the issue or provide borrower satisfaction. HUD believes that the addendum to the HUD–1 complements the proposed GFE by apprising the borrower as to whether the tolerances imposed by the proposed GFE have been met, thereby minimizing post-settlement questions as to any cost variances between the GFE and the HUD–1.

With respect to issues arising from the loan provided at settlement, the most frequent complaints stem from the following: The interest rate for the loan the borrower received was not the interest rate applied for; the borrower applied for a fixed rate loan but received an adjustable rate loan at settlement; and the closing documents were not explained to the borrower, leaving the borrower unaware or unsure of important loan information. In addition, HUD is aware that in many cases, borrowers are unaware of or confused by certain loan terms. This problem has become more acute with the rise of non-traditional mortgages. For example, many borrowers do not have a solid understanding of negative amortization or are unaware of the potential for negative amortization. For borrowers with adjustable rate loans, many do not understand the maximum amount their monthly mortgage payment could reach when the interest rate adjusts. In addition, many borrowers are unaware of the prepayment penalty in their loan until they try to refinance.

To address these issues, today's proposed rule would require the settlement agent or other person conducting the settlement to read the closing script document aloud to the borrower and explain: (1) The comparison between the loan terms and the settlement charges listed on the HUD–1/1A settlement form with the estimate of charges listed on the GFE; (2) whether or not the tolerances have been met; and (3) the loan terms, as contained in the mortgage note and related settlement information. Any inconsistencies between the mortgage note, between related settlement information and the GFE, and between the HUD–1/1A settlement charges and the GFE would have to be disclosed and explained to the borrower. The proposed rule would also require that the closing script addendum be delivered to the borrower as part of the HUD–1/1A at the closing. Upon request of the borrower, the HUD–1/1A and the closing script addendum would have to be made available for review by the borrower 24 hours prior to the settlement, in accordance with 24 CFR 3500.10.

The instructions to the preparer of the closing script are included in Appendix A to the rule. Examples of closing scripts are also provided in Appendix A to the rule. All instructions for completing the closing script are proposed to be codified with the rule at the final rule stage.

Enforcement. The Proposed Rule. The proposed rule provides that failure to complete the HUD–1 in accordance with the regulations constitutes a violation of Section 4 of RESPA.

H. Permissibility of Average Cost Pricing and Negotiated Discounts

The Proposed Rule. The proposed rule would recognize pricing mechanisms that result in greater competition and lower costs to consumers, specifically average cost pricing and some discounts among settlement service providers, including volume-based discounts. The proposed rule would amend 24 CFR 3500.8 and would explain that charges for third party services may be calculated using average cost pricing mechanisms based on appropriate methods established by HUD. These mechanisms would also accommodate certain volume-based discounts. Although the third party charge on any one loan may be higher than the average, the third party charge on another loan may be lower, provided that borrowers are being charged no more than the average price actually received by the third parties during the period on which the average price is computed. The proposed rule would allow loan originators to disclose on the HUD–1 an average cost price in accordance with one of several specific methods. The proposed rule would also amend 24 CFR 3500.14(d) and the definition of "thing of value" to clarify that it is permissible for settlement service providers to negotiate discounts in the prices for settlement services, so long as the borrower is not charged more than the discounted price. The practice of negotiating discounts in prices—whether among settlement service providers, such as with volume-based discounts, or by a settlement service provider on behalf of consumers—can serve to reduce prices to consumers.

Discussion. In this proposed rule, HUD is seeking to facilitate pricing arrangements that will benefit consumers. HUD has determined that in the evolving marketplace, certain loan originators and third party settlement service providers may wish to adopt average cost pricing and to offer

discounts, including volume-based discounts. HUD welcomes comment on these and any other pricing techniques that may result in greater competition and lower costs to consumers and that are consistent with the purposes of RESPA.

Congress authorized the Secretary, pursuant to Section 19(a) of RESPA, to prescribe such rules and regulations and to make such interpretations as may be necessary to achieve the purposes of RESPA. In enacting RESPA, Congress found that reforms in the real estate settlement process were needed to protect consumers from the unnecessarily high settlement charges that had evolved in some areas of the country. Congress explained the purpose of RESPA as being to effect changes in the residential settlement process that will result "in more effective advance disclosure to home buyers and sellers of settlement costs" and "the elimination of kickbacks or referral fees that tend to increase unnecessarily the costs of certain settlement services."

Congress sought to achieve its purposes through both prohibitions on conduct and better consumer disclosures. The Senate Committee Report on S.3164, the bill that was eventually enacted as RESPA, noted that the Committee on Housing, Banking, and Urban Affairs recommended an approach to the problems of settlement costs that would regulate the underlying business relationships and procedures of which the costs are a function, rather than regulating closing costs directly. (See S Rep. 93–866, at 3 (1974).) Through the prohibitions against kickbacks and unearned fees in Section 8 and the escrow account requirements in Section 10, the Senate Committee was aiming to ensure that the costs of buying a home would not be "unreasonably or unnecessarily inflated" (Id). In fact, the Committee expected that advance disclosure of settlement charges would reduce or eliminate many "unnecessary or unreasonably high settlement charges" (Id).

Section 4(a) of RESPA authorizes the Secretary to prescribe the primary disclosure document for settlement, the Uniform Settlement Statement, generally known as the HUD–1 (or HUD–1A) Settlement Statement. This standard form is used at settlement to disclose all charges imposed on the borrower and the seller. Section 4 is silent, however, on how such charges are calculated. Congress expressly encouraged flexibility on the application of at least some of the Section 4 requirements relating to the HUD–1 Settlement Statement, by allowing for the deletion from the form of items that are not required by local custom.

In Section 5(c) of RESPA, Congress required that the lender provide to the borrower "a good faith estimate of the amount or range of charges" that the borrower is likely to incur at settlement. Section 5, like Section 4, is silent on how such charges are to be calculated. This GFE of charges is to be included with a special information booklet that contains information about the homebuying and home finance process. Section 5(b)(1) of RESPA requires that the booklet include "a description and explanation of the nature and purpose of each cost incident to a real estate settlement," but does not require that each charge be calculated on a per-transaction cost basis. Section 8(c) of RESPA is evidence of the approach that regulates the underlying business relationships and procedures, in that it exempts specific kinds of business payments from being found to violate RESPA's prohibitions on kickbacks, referral fees, and unearned fees. Section 8(c)(1) establishes exemptions for payments between title companies and their agents, between lenders and their agents, and to attorneys, for services actually performed. Similar exemptions are established in subsections (c)(3) and (c)(4) for payments between real estate brokers and their agents, and among affiliated businesses. In section 8(c)(2), Congress permits settlement service providers to be compensated "for goods or facilities actually furnished [and] for services actually performed," without requiring a particular, regimented pricing structure.

Section 8(c)(5) of RESPA gives the Secretary discretion to permit "such other payments or classes of payments * * * as are specified in regulations prescribed by the Secretary, after consultation with [other Federal officials and entities]." Through this section and section 19, the Secretary has been given broad regulatory authority to address changes in the real estate marketplace under RESPA.

HUD's current regulations implementing RESPA have sometimes been cited as obstacles to consumer-friendly business practices, however. Discussions at the RESPA Reform Roundtables during 2005 and additional comments from both industry representatives and consumer advocates have suggested the need for greater competition among settlement service providers. In light of these suggestions, the Secretary has determined that, in HUD's implementation of RESPA, there should be greater flexibility for cost pricing formulas that bring more innovation and increased price competition to the settlement process. HUD proposes to recognize in the regulations that innovative approaches such as average cost pricing and certain discounts, including volume-based discounts, may serve to lower settlement costs to consumers without violating the statutory requirements of RESPA.

The practices of negotiating price reductions—whether among settlement service providers or by an individual settlement service provider on behalf of consumers—can serve to reduce prices to consumers. Such arrangements are not contrary to the purposes of RESPA and do not violate section 8 when any and all pricing benefits are passed on to consumers. Accordingly, in today's proposed rule, HUD is amending the definition of "thing of value" set forth in 24 CFR 3500.14(d) to exclude discounts negotiated by settlement service providers based on negotiated pricing arrangements, provided that no more than the reduced price is charged to the borrower and disclosed on the HUD–1/1A.

In the 2002 proposed rulemaking, in the context of loan originators being subject to tolerances for their GFE estimates of settlement service charges, HUD recognized that:

> [T]he new GFE's tighter requirements on estimated third party charges may cause many loan originators not already doing so to seek to establish pricing arrangements with specific third party settlement service providers in advance, in order both to ensure they are able to meet the tolerances and to ensure lower prices for their customers. As part of negotiations for such arrangements, many originators, particularly those with a substantial volume of business, may seek prices from third party providers that are lower than those providers offer on a retail basis. However, because Section 8 of RESPA broadly prohibits providing a "thing of value," which is specifically defined to include discounts, in exchange for the referral of business, many loan originators have been reluctant to openly seek such pricing benefits, even where any such discount in the price is passed on to the borrower. HUD believes that the fundamental purpose of RESPA is to lower settlement costs to borrowers, and it is therefore contrary to the law's objectives to interpret the anti-referral fee provisions of Section 8 to prohibit one settlement service provider from using its market power to negotiate discounted prices, as long as the entire discounted price negotiated by the originator is charged to the borrower and reported as part of the total charge. * * *

67 FR 49134, 49151 (July 29, 2002).

Lender comments on the 2002 Proposed Rule and discussions during the RESPA Reform Roundtables in 2005

continued to cite a need for a complete exemption from section 8 before lenders could use pricing models that would allow them to introduce more price competition in the marketplace. These comments were primarily in the context of the mortgage packaging proposal, however, and in 2002 HUD had proposed a "safe harbor" or section 8 exemption in that context. In advance of that proposal, HUD had determined that in order to fully develop the potential to reduce closing costs, loan originators would be able to seek discounts, including volume-based discounts, and to utilize average cost pricing. Today's proposed rule relies on adapting the GFE requirements to broaden the mortgage lending and settlement services marketplace, without a need for specific packaging proscriptions and requirements or a section 8 exemption.

HUD believes that no such exemption is necessary in order to permit average cost pricing and discounting, including volume-based discounts. Rather, HUD has determined that RESPA provides enough flexibility to permit a variety of approaches to fee calculations, so long as they do not unnecessarily increase fees charged to consumers. During the 2005 RESPA Roundtables, some loan originators and third party settlement service providers also took the position that neither a full section 8 exemption nor formal authority for packaging is needed. These providers believed that development of different pricing mechanisms and some discounts could promote market innovation and increased price competition.

In this rule, the Secretary is proposing to use the authority under section 19(a) of RESPA to permit pricing techniques using average cost pricing and certain discounts, consistent with RESPA's GFE and settlement statement requirements, and with section 8. HUD believes that consumers will ultimately benefit from negotiated pricing among and by settlement service providers. This proposed rule seeks to lower consumer costs by permitting settlement service providers who procure, or who help consumers to obtain, third party settlement services, to negotiate the pricing of those services by the third party provider. By using average cost pricing, settlement service providers could avoid having to track individual prices paid for third party services on a transaction-by-transaction basis, thereby lowering administrative costs that would be passed on to consumers.

The proposed rule would make clear that where average cost pricing is used, the evaluation of prices of third party services should focus on all of the loan originator's transactions together, rather than viewing each transaction separately. An individual borrower might be charged more or less than the actual amount paid for that service in an individual transaction, provided that borrowers are being charged no more than the average price actually received by third parties during the period in which the average price is computed.

The proposed rule sets forth two specific methods that loan originators may use to calculate an average price for a particular settlement service. The loan originator would designate a recent 6-month period as the "averaging period" for purposes of calculating the average price. The same average price must then be used in every transaction in that class of transactions for which a GFE is provided following the averaging period until a new averaging period is established. The average price would be calculated either as: (1) The actual average price for the settlement service during the averaging period; or (2) a projected average under a tiered pricing contract, based on the number of transactions that actually closed during the recent averaging period. If a loan originator uses one of these methods to calculate the average price for a settlement service, HUD will deem the loan originator to have complied with the requirements of the rule.

HUD welcomes comments on its proposed methods for calculating average cost prices and on any alternative methods that should be permitted. Specifically, HUD welcomes comments on how to define "class of transactions." For example, "class of transactions" could be defined by loan type, or loan-to-value ratio. HUD is also interested in suggestions on alternative average cost pricing methods and other pricing methods that benefit consumers and are based on factors that would lead to charges to the consumer (and the disclosure of such charges) that are easily calculated, verified, and enforced, but difficult to manipulate in an abusive manner. Such factors could include, for example:

(a) Experience over a period of time that is longer or shorter than that currently provided in the proposed rule;

(b) Prices for the service among the usual third party providers upon which the lender or other settlement service usually relies;

(c) General industry practices; and

(d) A reasonable projection of future costs.

Finally, with regard to any pricing method used by a settlement service provider, if a violation of section 8 of RESPA is alleged and an investigation ensues, the proposed rule would place the burden on the targeted settlement service provider to demonstrate compliance with a permissible pricing method through the production of relevant records.

I. Changes To Strengthen Prohibition Against Requiring the Use of Affiliates

The Proposed Rule. The proposed rule would change the definition of "required use" in § 3500.2, so that consumers would be more likely to shop for the homes and home features, and the loans and other settlement services, that are best for them, free from the influence of disingenuous referral arrangements. HUD intends the rule to establish that, in a real estate transaction covered by RESPA, incentives that consumers may want to accept and disincentives that consumers may want to avoid should be analyzed similarly for compliance with RESPA.

This change would make it clear that HUD views economic disincentives that a consumer can avoid only by purchasing a settlement service from particular providers or businesses to which the consumer has been referred to be potentially as problematic under RESPA as are economic incentives that are contingent on the consumer's choice of a particular settlement service provider. In particular, the change proposed today may affect the analysis under section 8(a) of disincentives that are avoided only by using an affiliated settlement service provider. The change may also affect sellers who use disincentives to influence a borrower's choice of a particular title company.

Consumer business captured through economic incentive or disincentive arrangements can raise questions about violations of section 8(a) of RESPA. The change proposed today may eliminate the argument by affiliated businesses that there is no "required use" that prevents them from invoking the affiliated business exemption to section 8 violations that involve consumer incentives and disincentives. The modifications in the proposed rule are not intended to prevent discounts that are beneficial to consumers, however. The revised definition states that the offering by a settlement service provider of an optional package or a combination of bona fide settlement services to a borrower at a total price lower than the sum of the prices of the individual settlement services would not constitute a "required use." By separate amendment to § 3500.14(d), such arrangements are defined as not being a thing of value, and so would not be in violation of the referral prohibitions in section 8(a) of RESPA.

The proposed revision to the "required use" definition would

continue to apply in two sections of the regulations: The affiliated business exemption in § 3500.15, and the prohibition on the seller requiring the buyer to purchase title insurance from a particular company in § 3500.16. However, as part of the proposed amendment of § 3500.7, and in light of other changes that would be made by this proposed rule, the term "required use" would no longer apply as it does currently in § 3500.7(e).

Discussion. Section 8(a) of RESPA prohibits persons from giving or receiving a thing of value, pursuant to an agreement for the referral of business incident to a settlement service in a covered transaction. RESPA was amended in 1983 to allow businesses to make referrals to affiliated businesses, however, and to receive a benefit from their ownership interest in the affiliated businesses, so long as three conditions are met (see section 8(c)(4)).[32] One of the three conditions is that affiliated businesses may not require consumers to use any particular provider of settlement services. The term "required use" is currently defined in § 3500.2 of HUD's regulations to mean a situation in which a person must use a particular provider of a settlement service in order to have access to some distinct service or property. In addition, the term appears in section 9 of RESPA [33], and in §§ 3500.7(e), 3500.14(f), 3500.15(b)(2), and 3500.16 of HUD's implementing regulations.

HUD believes that some businesses have used the affiliated business arrangement exception in section 8 of RESPA to steer consumers to affiliated settlement service providers that may not provide the best mortgage products or settlement services for those consumers. A number of such complaints stem from builders, who are in a position to refer settlement service business, that use incentives or penalties to steer consumers to the builders' affiliated mortgage and title companies. Consumers have frequently contacted HUD to express concerns and register complaints about these practices, which usually fall into one of two categories.

First, consumers complain that the cost to the builders of incentives and discounts related to the homes themselves have been built into the sales price of the homes, so that they are not true incentives and discounts, but are penalties (i.e., higher sales prices) that are imposed if the consumer chooses an unaffiliated settlement service provider. Second, consumers complain that the rates and fees charged by builders' affiliated settlement service providers are higher than what would be charged by unaffiliated settlement service providers. In both of these cases, consumers may be confused about the value of the "deal," and may forego shopping for lower rates and fees offered by unaffiliated settlement service providers.

For example, HUD has recently received complaints such as:

- A buyer was offered a $22,000 discount on the price of a home for using the builder's affiliated lender, but the interest rate offered by the lender was ½ point higher than the market rate, and the origination fee charged by the affiliated lender was higher.
- A buyer would be required to make a higher earnest money deposit and would lose a $2,000 "closing incentive" if the buyer did not use the builder's affiliated lender.
- A builder promised a $3,000 incentive on the purchase price and $6,000 toward closing costs if the buyer used the builder's affiliated lender, which charged an interest rate that was 1 percent higher than the market rate and additional fees.

The effect of the change made by the proposed rule in the definition of "required use" is not limited to builders and their affiliated settlement service providers. Any businesses that are either clearly affiliated because of their company structures, or that would be deemed to be in an "affiliated business arrangement" under RESPA's definitions of that term and the related term of "associate," should be aware of the change in the definition of "required use" in this proposed rule. This change could affect the applicability of the affiliated business requirements to those businesses.

Further, the definition applies to all sellers of property in RESPA covered transactions, for purposes of the prohibitions in section 9 of RESPA against requiring directly or indirectly that buyers purchase title insurance from any particular title company.

HUD is requesting comments on whether the proposed change in the definition of "required use" will better serve the purposes of RESPA and whether further improvements could be made in the definition to accomplish the intent of both the affiliated business exemption in section 8 and the prohibition in section 9 on the required use of a title company.

J. Technical Amendments to Current RESPA Regulations

The Proposed Rule. The proposed rule would update the current RESPA regulations concerning the provision of the mortgage servicing disclosure statement within 3 days of an application for a mortgage loan, to ensure consistency with current statutory requirements. In addition, the proposed rule would update the current escrow regulations, by removing outdated provisions.

Specifically, the proposed rule would amend current § 3500.21 to conform to the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (Title II of the Omnibus Consolidated Appropriations Act, 1997) (Pub. L. 104–208) (the Act). Section 2103(a) of the Act amended section 6(a) of RESPA to eliminate the requirement that applicants for federally related mortgage loans be provided a disclosure describing the lender's historical practice regarding the sale or transfer of servicing rights, and the requirement that loan applications contain signed statements from applicants acknowledging that they have read and understood the disclosure provided.

On May 9, 1997, the Department published a proposed rule (62 FR 25740) designed in part to modify HUD's existing RESPA regulations concerning the disclosure to mortgage borrowers of information pertaining to the lender's practices regarding the transfer or sale of servicing rights (RESPA section 6(a)), in order to make the regulations consistent with 1996 statutory amendments effected by the Economic Growth and Regulatory Paperwork Reduction Act. The Department received numerous comments on the proposed rule, and the comments were generally favorable. However, the Department never finalized that proposed rule. Due to the amount of time that has passed since the first proposed rule, today's proposed rule seeks comment on changes to conform the transfer of servicing disclosure requirements to the current statutory requirements.

In addition, the proposed rule would make changes to current § 3500.17 to eliminate the phase-in period for aggregate accounting for escrow accounts. The phase-in period was a transitional provision that expired on October 27, 1997. All servicers are currently required to use the aggregate accounting method. Today's proposed

[32] Section 8(c)(4) (12 U.S.C. 2607(c)(4)) of RESPA states in part that "Nothing in this section shall be construed as prohibiting * * * affiliated business arrangements so long as (A) a disclosure is made of the existence of such an arrangement to the person being referred * * *, (B) such person is not required to use any particular provider of settlement services, and (C) the only thing of value that is received from the arrangement, other than the payments permitted under this subsection, is a return on the ownership interest * * *."

[33] Section 9 states in part that "[n]o seller of property * * * shall require directly or indirectly, as a condition to selling the property, that title insurance covering the property be purchased by the buyer from any particular title company."

rule would clarify this by eliminating provisions from § 3500.17 that relate only to the alternate accounting methods that were permitted during the phase-in period.

K. ESIGN Applicability to RESPA Disclosures

The Proposed Rule. The proposed rule would amend HUD's RESPA rules to explicitly recognize the current statutory applicability of the Electronic Signatures in Global and National Commerce Act (ESIGN), 15 U.S.C. 7001–7031, to RESPA. This amendment is intended to make clear that all RESPA disclosures may be provided to consumers in electronic form, so long as the consumer consents to receive such disclosures in electronic form and the other specific conditions of ESIGN are met. This recognition of the applicability of ESIGN to RESPA would also make clear that all documents required to be retained under RESPA may be retained in electronic format, so long as the ESIGN requirements for document retention are met.

V. Questions for Commenters

HUD welcomes comments on all aspects of the proposal. In addition, HUD specifically requests comment on the following issues:

1. Whether a 12-month implementation period for the GFE is appropriate. (Section IV.D.)
2. The proposed GFE, as well as the proposed HUD–1/1A Settlement Statement Forms.
3. Possible additional ways to increase consumer understanding of adjustable rate mortgages.
4. Whether the proposed requirements for completing and delivering the Addendum to the HUD–1/1A, including the mandatory reading of the Closing Script by the party conducting the closing to the borrower(s), are the best methods for assuring that borrower(s) understand their loan terms and the differences between the GFE and the HUD–1/1A.
5. Whether a provision should be added to the RESPA regulations allowing a loan originator, for a limited time after closing, to address the failure to comply with tolerances under the proposed GFE requirements, and if so, how should such a provision be structured? (Section IV.E. 10) Would such a provision be useful, and if so, what would be the appropriate time frame for finding and refunding excess charges? Could such a provision be abused, and therefore harmful to consumers? Would the ability of prosecutors to exercise enforcement discretion obviate the need for such a provision?
6. Proposed methods for calculating average cost prices and on any alternative methods that should be permitted. (Section IV.H.) Specifically, how to define "class of transactions." Comments are also invited on alternative average cost pricing methods and other pricing methods that benefit consumers and are based on factors that would lead to charges to the consumer and disclosure of such charges that are easily calculated, verified, and enforced, but difficult to manipulate in an abusive manner. Such factors could include:

(a) Experience over a period of time that is longer or shorter than that currently provided in the proposed rule;

(b) Prices for the service among the usual third party providers upon which the lender or other settlement service usually relies;

(c) General industry practices; and

(d) A reasonable projection of future costs.

7. Whether the proposed change in the definition of "required use" will better serve the purposes of RESPA and whether further improvements could be made in the definition to accomplish the intent of both the affiliated business exemption in section 8 and the prohibition in section 9 on the required use of a title company. (Section IV.I.)
8. With respect to the revised definition of "Good Faith Estimate" set forth in the proposed rule language at 24 CFR 3500.2, is the standard set forth sufficient to ensure that good faith estimates will be filled out consistently by all loan originators in a particular community?
9. Should the Section 6 disclosure on transfer of servicing that is required under RESPA be included on the GFE?
10. Should a loan originator be required to include a "no cost loan" on the trade-off chart on page 3 of the GFE as one of the alternative loans if it is not the loan for which the GFE is written?

VI. Findings and Certifications

The Paperwork Reduction Act

Information Collection Requirements

The information collection requirements contained in this proposed rule have been submitted to the Office of Management and Budget (OMB) under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501–3520). In accordance with the Paperwork Reduction Act, an agency may not conduct or sponsor, and a person is not required to respond to, a collection of information, unless the collection displays a currently valid OMB control number.

The burden of the information collections in this proposed rule is estimated as follows:

REPORTING AND RECORDKEEPING BURDEN

Information collection	Number of respondents	Frequency of response	Responses per annum	Burden hour per response	Annual burden hours	Hourly cost	Annual cost
GFE/Information Booklet	50,000	425	21,250,000	0.17	5,3,612,500	$31.14	$112,493,250
Servicing Disclosure	0	0	0	0	0	0	0
Transfer Disclosure	20,000	3,000	60,000,000	0.03	1,800,000	10.00	18,000,000
HUD–1 or HUD–1A and Closing Script	20,000	625	12,500,000	0.58	7,250,000	33.74	244,615,000
Initial Escrow	2,000	4,875	9,750,000	0.08	780,000	*0.00	0
Annual Escrow	2,000	21,100	42,200,000	0.08	3,376,000	*20.00	67,520,000
Voluntary Escrow Account Payments	2,000	600	1,200,000	0.08	99,600	20.00	1,920,000
AfBA	10,000	269	2,689,500	0.10	268,950	20.00	5,379,000
Totals			149,589,500		17,183,450		$449,927,250

In accordance with 5 CFR 1320.8(d)(1), HUD is soliciting comments from members of the public and affected agencies concerning this collection of information to:

(1) Evaluate whether the proposed collection of information is necessary for the proper performance of the functions of the agency, including whether the information will have practical utility;

(2) Evaluate the accuracy of the agency's estimate of the burden of the proposed collection of information;

(3) Enhance the quality, utility, and clarity of the information to be collected; and

(4) Minimize the burden of the collection of information on those who are to respond; including through the use of appropriate automated collection techniques or other forms of information technology, e.g., permitting electronic submission of responses.

Interested persons are invited to submit comments regarding the information collection requirements in this rule. Under the provisions of 5 CFR part 1320, OMB is required to make a decision concerning this collection of information between 30 and 60 days after today's publication date. Therefore, a comment on the information collection requirements is best assured of having its full effect if OMB receives the comment within 30 days of today's publication. Comments must refer to the proposal by name and docket number (FR–5180) and must be sent to: HUD Desk Officer, Office of Management and Budget, New Executive Office Building, Washington, DC 20503, Fax number: (202) 395–6947 and Reports Liaison Officer, Office of Housing—Federal Housing Commissioner, Department of Housing and Urban Development, 451 Seventh Street, SW., Room 9136, Washington, DC 20410–8000.

Environmental Impact

A Finding of No Significant Impact with respect to the environment has been made in accordance with HUD regulations at 24 CFR part 50, which implement section 102(2)(C) of the National Environmental Policy Act of 1969 (42 U.S.C. 4332(2)(C)). The Finding of No Significant Impact is available for public inspection between the hours of 8 a.m. and 5 p.m. weekdays in the Regulations Division, Office of General Counsel, U.S. Department of Housing and Urban Development, 451 Seventh Street, SW., Room 10276, Washington, DC 20410–0500. Due to security measures at the HUD Headquarters building, an advance appointment to review the public comments must be scheduled by calling the Regulations Division at (202) 402–3055 (this is not a toll-free number). Individuals with speech or hearing impairments may access this number via TTY by calling the toll-free Federal Information Relay Service at (800) 877–8339.

Executive Order 12866, Regulatory Planning and Review

OMB reviewed this proposed rule under Executive Order 12866 (entitled "Regulatory Planning and Review"), which the President issued on September 30, 1993. This rule was determined economically significant under the executive order. Any changes made to the proposed rule subsequent to its submission to OMB are identified in the docket file, which is available for public inspection in the Regulations Division, Office of General Counsel, U.S. Department of Housing and Urban Development, 451 Seventh Street, SW., Room 10276, Washington, DC 20410–0500. The Initial Economic Analysis prepared for this rule is available online at *http://www.hud.gov/respa*, and for public inspection in the Regulations Division. Due to security measures at the HUD Headquarters building, an advance appointment to review the public comments must be scheduled by calling the Regulations Division at (202) 402–3055 (this is not a toll-free number). Individuals with speech or hearing impairments may access this number through TTY by calling the Federal Information Relay Service at (800) 877–8339.

Federalism Impact

This proposed rule does not have federalism implications and does not impose substantial direct compliance costs on state and local governments or preempt state law within the meaning of Executive Order 13132 (entitled "Federalism").

Regulatory Flexibility Act

The Secretary, in accordance with the Regulatory Flexibility Act (5 U.S.C. 605(b)), has reviewed and approved this proposed rule and has determined that the rule would have a significant economic impact on a substantial number of small entities within the meaning of the Regulatory Flexibility Act.

In accordance with section 603 of the Regulatory Flexibility Act, an Initial Regulatory Flexibility Analysis (IRFA) has been prepared and has been made part of the Economic Analysis prepared under Executive Order 12866. The IRFA portion, however, of the combined analysis is published as an appendix to this proposed rule. The IRFA was also submitted to the Chief Counsel for Advocacy of the Small Business Administration for review and comment on its impact on business.

Unfunded Mandates Reform Act

Title II of the Unfunded Mandates Reform Act of 1995 (2 U.S.C. 1531–1538) (UMRA) requires federal agencies to assess the effects of their regulatory actions on state, local, and tribal governments and on the private sector. This proposed rule does not, within the meaning of the UMRA, impose any federal mandates on any state, local, or tribal governments nor on the private sector.

Congressional Review of Final Rules

This rule constitutes a "major rule" as defined in the Congressional Review Act (5 U.S.C. Chapter 8). At the final rule stage, this rule will have a 60-day delayed effective date and be submitted to the Congress in accordance with the requirements of the Congressional Review Act.

List of Subjects

24 CFR Part 203

Hawaiian Natives, Home improvement, Indians—lands, Loan programs—housing and community development, Mortgage insurance, Reporting and recordkeeping requirements, Solar energy.

24 CFR Part 3500

Consumer protection, Condominiums, Housing, Mortgagees, Mortgage servicing, Reporting, and Recordkeeping requirements.

For the reasons stated in the preamble, HUD proposes to amend 24 CFR parts 203 and 3500 as follows:

PART 203 — SINGLE FAMILY MORTGAGE INSURANCE

1. The authority citation for part 203 continues to read as follows:

Authority: 12 U.S.C. 1709, 1710, 1715b, 1715z–16, and 1715u; 42 U.S.C. 3535(d).

2. In § 203.27, paragraph (a)(2) is revised to read as follows:

§ 203.27 Charges, fees, or discounts.

(a) * * *

(2) A charge to compensate the mortgagee for expenses incurred in originating and closing the loan, *provided* that the Commissioner may establish limitations on the amount of any such charge.

* * * * *

PART 3500—REAL ESTATE SETTLEMENT PROCEDURES ACT

3. The authority citation for part 3500 continues to read as follows:

Authority: 12 U.S.C. 2601 *et seq.*; 42 U.S.C. 3535(d).

4. In § 3500.2, paragraph (b) is amended by removing the definition of Application; revising the definitions of *Good faith estimate or GFE, Mortgage broker*, and *Required use* and add, in alphabetical order, the following new definitions of *Adjustable rate, Balloon payment, Closing script, Credit or charge for the specific interest rate chosen, Good faith estimate applicant or GFE applicant, Good faith estimate application or GFE application, Loan originator, Mortgage application, Origination service, Prepayment penalty, Primary title service, Third party, Tolerance, and Unforeseeable circumstances* to read as follows:

§ 3500.2 Definitions.

* * * * *

(b) * * *

Adjustable rate has the same meaning as "adjustable rate" under the Truth in Lending Act, 15 U.S.C. 1601 *et seq.* ("TILA").

Balloon payment has the same meaning as "balloon payment" under the Truth in Lending Act, 15 U.S.C. 1601 *et seq.* ("TILA").

* * * * *

Closing script means the disclosure document prepared for the closing by the settlement agent, pursuant to information provided by the loan originator, that compares the loan terms and settlement charges estimated on the GFE with the HUD–1/HUD–1A and that describes, in detail, the required loan terms for the specific mortgage loan and related settlement information. It is an addendum to the HUD–1/HUD–1A.

Credit or charge for the specific interest rate chosen means, for a mortgage broker, the credit or charge for the specific interest rate chosen is the difference between the initial loan amount and the payment to the mortgage broker (i.e., the sum of the price paid for the loan by the lender and any other payments to the mortgage broker from the lender). When the amount paid to the mortgage broker exceeds the initial loan amount, there is a credit to the borrower and it is entered as a negative amount in block 2 of the GFE. When the initial loan amount exceeds the amount paid to the mortgage broker, there is a charge to the borrower and it is entered as a positive amount in block 2 of the GFE.

* * * * *

Good faith estimate or *GFE* means an estimate of settlement charges a borrower is likely to incur, as a dollar amount, and related loan information, based upon common practice and experience in the locality of the mortgaged property, provided on the form prescribed in Appendix C to this part that is prepared in accordance with § 3500.7 and the Instructions in Appendix C to this part.

Good faith estimate applicant or *GFE applicant* means any prospective borrower for a federally related mortgage loan who submits a GFE application.

Good faith estimate application or *GFE application* means a written or oral submission to a loan originator by a prospective borrower to obtain a GFE for a specific loan product. The loan originator may require the GFE applicant to provide no more than the prospective borrower's name, Social Security number, property address, monthly income, the borrower's best estimate of the value of the property, and the mortgage loan amount sought by the borrower to obtain a GFE. A GFE application shall either be in writing or electronically submitted, including a written record of an oral application, so that the loan originator can retain a record of the application. If the submission does not state or identify a specific property, the submission is not a GFE application. The subsequent addition of an identified property to the submission converts the submission to a GFE application. Neither a GFE application nor an application for a prequalification is a mortgage application for a federally related mortgage under this part.

* * * * *

Loan originator means a lender or mortgage broker.

* * * * *

Mortgage application means a submission to a loan originator by a prospective borrower of such financial and other information, whether written or computer-generated, as a loan originator may require to begin final underwriting, and such other steps as are necessary to originate a mortgage loan for the prospective borrower.

Mortgage broker means a person (not an employee of a lender) or entity that renders origination services in a table funded or intermediary transaction. A loan correspondent approved under 24 CFR 202.8 for Federal Housing Administration programs is a mortgage broker for purposes of this part.

* * * * *

Origination service means any service involved in the creation of a mortgage loan, including but not limited to the taking of loan applications, loan processing, and the underwriting and funding of loans, and the processing and administrative services required to perform these functions.

* * * * *

Prepayment penalty has the same meaning as "prepayment penalty" under the Truth in Lending Act, 15 U.S.C. 1601 *et seq.* ("TILA").

Primary title service means any service involved in the provision of title insurance (lender or owner policy) and settlement or closing services, including but not limited to: title examination and evaluation; preparation and issuance of title commitment; clearance of underwriting objections; preparation and issuance of a title insurance policy or policies; and the processing and administrative services required to perform these functions.

* * * * *

Required use means a situation in which a borrower's access to some distinct service, property, discount, rebate, or other economic incentive, or the borrower's ability to avoid an economic disincentive or penalty, is contingent upon the borrower using or failing to use a referred provider of settlement services. However, the offering by a settlement service provider of an optional combination of *bona fide* settlement services to a borrower at a total price lower than the sum of the prices of the individual settlement services does not constitute a required use.

* * * * *

Third party means a settlement service provider other than a loan originator.

* * * * *

Tolerance means the maximum amount by which the charge for a category or categories of settlement costs may exceed the amount of the estimate for such category or categories on a GFE.

Unforeseeable circumstances means:

(1) Acts of God, war, disaster, or other emergency making it impossible or impracticable for the loan originator to complete the transaction; and

(2) Circumstances that could not be reasonably foreseen by a loan originator at the time of GFE application that are particular to the transaction and that result in increased costs, such as a change in the property purchase price, boundary disputes, the need for a second appraisal or flood insurance, or environmental problems. Market fluctuations by themselves shall not be considered unforeseeable circumstances.

§ 3500.6 [Amended]

5. Section 3500.6 is amended in paragraph (a) introductory text by adding "GFE or a" before "federally related mortgage loan", and in paragraph (a)(1) by adding "GFE" before the word "application" the first time it appears.

6. In § 3500.7, the section heading and paragraphs (a) through (e) are revised; paragraph (f) is redesignated as paragraph (g); and new paragraphs (f) and (h) are added, as follows:

§ 3500.7 Good faith estimate or GFE.

(a) *Lender to provide.* (1) Except as otherwise provided in paragraphs (a), (b), or (g) of this section, not later than 3 business days after a lender receives a GFE application from a GFE applicant, or information sufficient to complete a GFE application, the lender must provide the GFE applicant with a GFE. In the case of dealer loans, the lender must either provide the GFE or ensure that the dealer provides the GFE.

(2) The lender must provide the GFE to the GFE applicant by hand delivery, by placing it in the mail, or, if the GFE applicant agrees, by fax, email, or other electronic means.

(3) The lender is not required to provide the GFE applicant with a GFE if, before the end of the 3-business-day period:

(i) The lender denies the GFE application of the GFE applicant;

(ii) The lender denies the mortgage application of the GFE applicant; or

(iii) The applicant withdraws its GFE application.

(4) The lender is not permitted to collect, as a condition for providing a GFE, any fee for an appraisal, inspection, or other similar service needed for final underwriting. The lender may, at its option, collect a fee limited to the cost of providing the GFE, including the cost of an initial credit report.

(b) *Mortgage broker to provide.* (1) Except as otherwise provided in paragraphs (b) or (g) of this section, either the lender or the mortgage broker must provide a GFE to the GFE applicant not later than 3 business days after a mortgage broker receives from the GFE applicant either a GFE application or information sufficient to complete a GFE application. The lender is responsible for ascertaining whether the GFE has been provided. If the mortgage broker has provided a GFE that is acceptable to the lender, the lender is not required to provide an additional GFE.

(2) The mortgage broker must provide the GFE by hand delivery, by mail, or, if the applicant agrees, by fax, email, or other electronic means.

(3) The mortgage broker is not required to provide the GFE applicant with a GFE if, before the end of the 3-business-day period:

(i) The mortgage broker or lender denies the GFE application of the GFE applicant;

(ii) The mortgage broker or lender denies the mortgage application of the GFE applicant; or

(iii) The applicant withdraws its GFE application.

(4) The mortgage broker is not permitted to collect, as a condition for providing a GFE, any fee for an appraisal, inspection, or other similar service needed for final underwriting. The mortgage broker may, at its option, collect a fee limited to the cost of providing the GFE, including the cost of an initial credit report.

(c) *Availability of GFE terms.* The estimate of the charges for all settlement services other than the charge or credit for the interest rate chosen, the adjusted origination charges, and per diem interest must be available until 10 business days from when the GFE is delivered, but it may remain available longer, if the loan originator extends the period of availability. Once a mortgage application is submitted to the loan originator, the non-interest rate-dependent settlement charges of the GFE that is the basis for the mortgage application must remain in effect until closing. If the interest rate was not locked when the mortgage application was submitted, or a locked interest rate has expired, all interest rate-dependent charges and disclosures may change. If the GFE applicant notifies the loan originator to proceed with a mortgage application after the period of availability has expired, the loan originator may:

(1) Continue to abide by the terms and conditions contained within the GFE for which the period of availability has expired;

(2) Deny the GFE applicant an opportunity to submit a mortgage application at that time for that specific loan because the applicant did not respond within the period of availability; or

(3) Provide a new GFE for a new loan to the GFE applicant within 3 business days.

(d) *Content and form of GFE.* The loan originator must prepare the GFE in accordance with the requirements of this section and the Instructions in Appendix C to this part when preparing the GFE Form in Appendix C to this part. The instructions in Appendix C to this part allow for flexibility in the preparation and distribution of the GFE in hard copy and electronic format.

(e) *Tolerances for amounts included on GFE.* (1) Absent unforeseeable circumstances, the actual charges at settlement may not exceed the amounts included on the GFE for:

(i) The loan originator's service charge;

(ii) While the borrower's interest rate is locked, the credit or charge for the interest rate chosen;

(iii) While the borrower's interest rate is locked, the adjusted origination charge; and

(iv) Government recording and transfer charges.

(2) Absent unforeseeable circumstances, the sum of the charges at settlement for the following services may not be greater than 10 percent above the sum of the amounts included on the GFE:

(i) Lender-required settlement services, where the lender selects the third party settlement service provider; and

(ii) Lender-required services, and optional owner's title insurance selected by the borrower, when the borrower uses a settlement service provider identified by the loan originator.

(3) The amounts charged for all other settlement services included on the GFE may change at settlement.

(4) If a loan originator cannot meet the tolerances under this section because of unforeseeable circumstances, the loan originator must document the unforeseeable circumstances that resulted in the increased costs and charge the borrower only the amount of the increased costs. In such situations, the loan originator must notify the borrower within 3 business days of the increase in charges arising from the unforeseeable circumstances, and a new GFE reflecting the revised charges must be provided to the borrower.

(5) Loan originators must retain documentation of any unforeseeable circumstances resulting in final costs in excess of the established tolerances for amounts stated on GFEs for no less than 3 years after settlement.

(f) *Changes to the GFE.* (1) The loan originator must complete final underwriting within a reasonable time after a borrower's mortgage application is complete. If final underwriting or unforeseeable circumstances result in a change in the borrower's eligibility for the specific loan terms identified in the GFE, the loan originator must:

(i) Notify the borrower within one business day of the decision to reject the loan;

(ii) If another loan is made available, provide a revised GFE to the borrower; and

(iii) Document the reasons for the revised GFE and retain the documentation for no less than 3 years after settlement.

(2) If a borrower requests changes to the mortgage loan identified in the GFE that change the settlement charges or the terms of the loan, the loan originator is no longer bound by the GFE, and the loan originator must:

(i) Notify the borrower within one business day of the decision to reject the loan;

(ii) If another loan is made available, provide a revised GFE to the borrower; and

(iii) Document the reasons for the revised GFE and retain the documentation for no less than 3 years after settlement.

(3) In transactions involving new home purchases, where settlement is anticipated to occur more than 60 days from the time of a GFE application, the loan originator may provide the GFE to the borrower with a clear and conspicuous disclosure stating that at any time up until 60 days prior to closing, the loan originator may issue a revised GFE. If no such separate disclosure is provided, the loan originator cannot issue a revised GFE, except as otherwise provided in paragraph (f) of this section.

* * * * *

(h) *Violations of section 5 of RESPA (12 U.S.C. 2604).* A loan originator that violates the requirements of this section, including by exceeding the charges listed on the GFE at settlement by more than the permitted tolerances, shall be deemed to have violated section 5 of RESPA.

7. In § 3500.8, paragraphs (b) and (c) are revised; and new paragraphs (d) and (e) are added to read as follows:

§ 3500.8 Use of HUD–1 or HUD–1A settlement statements.

* * * * *

(b) *Charges to be stated.* The settlement agent shall complete the HUD–1 or HUD–1A in accordance with the instructions set forth in Appendix A to this part.

(1) *In general.* The settlement agent shall state the actual charges paid by the borrower and seller on the HUD–1 or HUD–1A. The settlement agent must separately itemize each third party charge paid by the borrower and seller. Origination services performed by or on behalf of the loan originator must be included in the loan originator's own charge. Primary title services performed by or on behalf of the title underwriter or title agent must be included in the title underwriter's or title agent's own charge. The amount stated on the HUD–1 or HUD–1A for any itemized service cannot exceed the amount actually received by the third party for that itemized service, unless the charge is based on an average cost price in accordance with paragraph (b)(2) of this section.

(2) *Average cost pricing.* (i) The charge shown on the HUD–1 or HUD–1A for a settlement service provided by a third party may be an average price calculated based on either of the following methods:

(A) The average price used on a HUD–1 or HUD–1A may be based on the actual average price for that service in all loans closed by the loan originator, on a national or more limited basis, during the averaging period; or

(B) The average price used on a HUD–1 or HUD–1A may be based on a tiered pricing contract, provided the projected number of loans used in calculating the average is equal to the number of loans actually closed by the loan originator during the averaging period.

(ii) For purposes of calculating an average price, the averaging period must be a specific recent period of 6 consecutive months preceding the receipt of a GFE application, as designated by the loan originator. The same method of determining the averaging period must be used for each borrower from whom a GFE application is received, until such time as the average is recomputed.

(iii) If a loan originator uses average cost pricing for any class of transactions in a particular period, the loan originator must use the same average cost price in every transaction within that class for which a borrower's GFE application was received during that period.

(iv) The loan originator must retain all documentation that the average cost pricing is accurate in a given time period, under the pricing formula used, for at least 3 years.

(c) *Aggregate accounting at settlement.* After itemizing individual deposits in the 1000 series, the servicer must make an adjustment based on aggregate accounting. This adjustment equals the difference in the deposit required under aggregate accounting and the sum of the itemized deposits. The computation steps for aggregate accounting are set out in § 3500.17(d). The adjustment will always be a negative number or zero (-0-). The settlement agent shall enter the aggregate adjustment amount on a final line in the 1000 series of the HUD–1 or HUD–1A statement. Appendix E to this part sets out an example of aggregate analysis. Appendix A to this part contains instructions for completing the HUD–1 or HUD–1A settlement statements using an aggregate analysis adjustment.

(d) *Closing script.* (1) The loan originator must transmit to the settlement agent all information necessary to complete the prescribed closing script disclosure document, which is an addendum to the HUD–1/1A settlement form and is prepared by the settlement agent. This addendum must accurately reflect the required information provided by the loan originator regarding the loan terms and related settlement information.

(2) The settlement agent or other person conducting the closing must read the closing script aloud to the borrower and explain:

(i) The comparison between the final settlement charges listed on the HUD–1/1A settlement form and the estimate of charges listed on the GFE;

(ii) Whether or not the tolerances have been met; and

(iii) Other required loan information as shown on the closing script addendum forms in Appendix A to this part.

(3) Any inconsistencies between the loan documents (including the mortgage note) and the summary of loan terms on the GFE, and between the HUD–1/1A settlement charges and the charges stated on the GFE, must be disclosed and explained to the borrower.

(4) Upon request of the borrower, the HUD–1/1A and the closing script addendum must be made available for review by the borrower 24 hours prior to the closing in accordance with § 3500.10(a). The closing script addendum must be delivered to the borrower with the HUD–1/1A at the closing in accordance with § 3500.10(a) and (c). The prescribed closing script addendum formats, with instructions, are set forth in Appendix A to this part.

(e) *Violations of section 4 of RESPA (12 U.S.C. 2604).* A violation of any of the requirements of this section will be deemed to be a violation of section 4 of RESPA.

§ 3500.10 [Amended].

8. Section 3500.10 is amended by adding the phrase ", with addendum," as follows:

a. In paragraph (a) after the word "statement";

b. In paragraph (b) after the reference "HUD–1A" in the first and last sentences; and

c. In paragraphs (c), (d), and (e) after each reference to "HUD–1A".

9. In § 3500.14, the text after the heading in paragraph (d) is redesignated

as paragraph (d)(1), and new paragraph (d)(2) is added, to read as follows:

§ 3500.14 Prohibition against kickbacks and unearned fees.

* * * * *

(d) Thing of value. (1) * * *

(2) A discount negotiated by settlement service providers in the price of a third party settlement service is not a thing of value, provided that no more than the discounted price is charged to the borrower and disclosed on the HUD–1/1A.

* * * * *

10. Section 3500.17 is amended:

a. In paragraph (b) by removing the definitions of *Acceptable accounting method, Conversion date, Phase-in period, Post-rule account,* and *Pre-rule account;*

b. In paragraph (c) by revising the heading and paragraphs (c)(4), (5), (6), and (8);

c. In paragraph (d) by removing paragraph (d)(2), redesignating paragraph (d)(1) as paragraph (d)(2), revising newly designated paragraph (d)(2)(i) introductory text, and redesignating the introductory text as paragraph (d)(1) and revising it; and

d. In paragraph (e) by removing paragraph (e)(3), to read as follows:

§ 3500.17 Escrow accounts.

* * * * *

(c) *Limits on payments to escrow accounts.* * * *

(4) *Aggregate accounting required.* All servicers must use the aggregate accounting method in conducting escrow account analyses.

(5) *Cushion.* The cushion must be no greater than one-sixth (1/6) of the estimated total annual disbursements from the escrow account.

(6) *Restrictions on pre-accrual.* A servicer must not practice pre-accrual.

* * * * *

(8) *Provisions in mortgage documents.* The servicer must examine the mortgage loan documents to determine the applicable cushion for each escrow account. If the mortgage loan documents provide for lower cushion limits, then the terms of the loan documents apply. Where the terms of any mortgage loan document allow greater payments to an escrow account than allowed by this section, then this section controls the applicable limits. Where the mortgage loan documents do not specifically establish an escrow account, whether a servicer may establish an escrow account for the loan is a matter for determination by State law. If the mortgage loan document is silent on the escrow account limits and a servicer establishes an escrow account under State law, then the limitations of this section apply unless State law provides for a lower amount. If the loan documents provide for escrow accounts up to the RESPA limits, then the servicer may require the maximum amounts consistent with this section, unless an applicable State law sets a lesser amount.

* * * * *

(d) *Methods of escrow account analysis.* (1) The following sets forth the steps servicers must use to determine whether their use of aggregate analysis conforms with the limitations in § 3500.17(c)(1). The steps set forth in this section result in maximum limits. Servicers may use accounting procedures that result in lower target balances. In particular, servicers may use a cushion less than the permissible cushion or no cushion at all. This section does not require the use of a cushion.

(2) *Aggregate analysis.* (i) In conducting the escrow account analysis using aggregate analysis, the target balances may not exceed the balances computed according to the following arithmetic operations:

* * * * *

11. Section 3500.21 is amended by revising paragraphs (b) and (c) to read as follows:

§ 3500.21 Mortgage servicing transfers.

* * * * *

(b) *Servicing Disclosure Statement; Requirements.* (1) At the time a GFE application for a mortgage servicing loan is submitted, or within 3 business days after submission of the GFE application, the lender, mortgage broker who anticipates using table funding, or dealer who anticipates a first lien dealer loan shall provide to each person who applies for such a loan a Servicing Disclosure Statement. A format for the Servicing Disclosure Statement appears as Appendix MS–1 to this part. The specific language of the Servicing Disclosure Statement is not required to be used. The information set forth in "Instructions to Preparer" on the Servicing Disclosure Statement need not be included with the information given to applicants, and material in square brackets is optional or alternative language. The model format may be annotated with additional information that clarifies or enhances the model language. The lender, table funding mortgage broker, or dealer should use the language that best describes the particular circumstances.

(2) The Servicing Disclosure Statement must indicate whether the servicing of the loan may be assigned, sold, or transferred to any other person at any time while the loan is outstanding. If the lender, table funding mortgage broker, or dealer in a first lien dealer loan will not engage in the servicing of the mortgage loan for which the applicant has applied, the disclosure may consist of a statement that such entity intends to assign, sell, or transfer servicing of such mortgage loan before the first payment is due. Alternatively, if the lender, table funding mortgage broker, or dealer in a first lien dealer loan will engage in the servicing of the mortgage loan for which the applicant has applied, the disclosure may consist of a statement that the entity will service such loan and does not intend to sell, transfer, or assign the servicing of the loan.

(c) *Servicing Disclosure Statement; Delivery.* The lender, table funding mortgage broker, or dealer that anticipates a first lien dealer loan shall deliver Servicing Disclosure Statements to each applicant for a mortgage servicing loan at the time a GFE application is received, or by placing it in the mail with prepaid first-class postage within 3 business days from receipt of the GFE application. In the event the borrower is denied credit within the 3 business-day period, no servicing disclosure statement is required to be delivered. If co-applicants indicate the same address on their GFE application, one copy delivered to that address is sufficient. If different addresses are shown by co-applicants on the GFE application, a copy must be delivered to each of the co-applicants.

* * * * *

12. A new § 3500.22 is added to read as follows:

§ 3500.22 Severability.

If any particular provision of this part or the application of any particular provision to any person or circumstance is held invalid, the remainder of this part and the application of such provisions to other persons or circumstances shall not be affected by such holding.

13. A new § 3500.23 is added to read as follows:

§ 3500.23 ESIGN applicability.

The Electronic Signatures in Global and National Commerce Act ("ESIGN"), 15 U.S.C. 7001–7031, shall apply to this part.

14. Appendix A to part 3500 is amended:

a. By revising the first two sentences of the first paragraph of the Appendix;

b. By removing the second paragraph of the General Instructions and adding four new paragraphs in its place;

c. By revising the first paragraph after the heading "Section L. Settlement Charges";

d. By revising the paragraphs for "Line 801" through "Lines 808–811" after the heading "Section L. Settlement Charges";

e. By revising the second paragraph and removing the third paragraph of instructions for "Lines 1000–1008" after the heading "Section L. Settlement Charges", and by removing the heading for the instructions for "Lines 1000–1008" and adding in its place "Lines 1000–1009";

f. By removing the paragraphs for "Lines 1100–1113" through "Lines 1111–1113" after the heading "Section L. Settlement Charges" and adding in their place nine paragraphs of instructions for lines 1100–1114;

g. By removing the paragraph for "Lines 1201–1205" after the heading "Section L. Settlement Charges" and adding in its place two paragraphs of instructions for lines 1200–1205;

h. By removing the paragraphs for "Lines 1301 and 1302" and for "Lines 1303–1305" after the heading "Section L. Settlement Charges" and adding in their place a paragraph of instructions for lines 1301–1305;

i. By revising the paragraph for "Line 1400";

j. By revising the first sentence in the first paragraph following the heading "Line Item Instructions for Completing HUD–1A";

k. By adding after the paragraph of instructions for "Line 1604" a new heading "General Instructions for Completing Closing Script Addendum to HUD–1/1A Settlement Form" and a new paragraph of instructions;

l. By revising the Forms "Settlement Statement" and "Settlement Statement Optional Form for Transactions without Sellers"; and

m. By adding new Instructions to Closing Script Preparer and Examples of Completed Closing Scripts 1 through 6, as follows:

APPENDIX A TO PART 3500—INSTRUCTIONS FOR COMPLETING HUD–1 AND HUD–1A SETTLEMENT STATEMENTS; SAMPLE HUD–1 AND HUD–1A STATEMENTS

The following are instructions for completing sections A through L and the closing script addendum of the HUD–1 settlement statement, required under section 4 of RESPA and Regulation X of the Department of Housing and Urban Development (24 CFR part 3500). This form is to be used as a statement of actual charges and adjustments paid by the borrower and the seller and received by each settlement service provider, to be given to the parties in connection with the settlement. * * *

General Instructions

* * * * *

The settlement agent shall complete the HUD–1 to itemize all charges imposed upon the Borrower and the Seller by the loan originator and all sales commissions, whether to be paid at settlement or outside of settlement, and any other charges which either the Borrower or the Seller will pay at settlement. For all items except for those paid to and retained by the loan originator, the name of the person or firm ultimately receiving the payment must be shown together with the total amount paid to such person in connection with the transaction. Charges that are customarily paid for by the seller must be shown in the seller's column on page 2 of the HUD–1 (unless paid outside closing), and charges that are customarily paid for by the borrower must be shown in the borrower's column (unless paid outside closing). If a seller pays for a charge that is customarily paid for by the borrower, the charge should not be shown on page 2 of the HUD–1 but instead should be listed as an adjustment in lines 506–509 of the HUD–1. If a borrower pays for a charge that is customarily paid for by the seller, the charge should not be shown on page 2 of the HUD–1, but instead should be listed as an adjustment in lines 204–209 of the HUD–1.

Charges to be paid outside of settlement by the borrower, seller, or loan originator, including cases where a non-settlement agent (i.e., attorneys, title companies, escrow agents, real estate agents, or brokers) holds the Borrower's deposit toward the sales price (earnest money) and applies the entire deposit towards the charge for the settlement service it is rendering, must be included on the HUD–1 but marked "P.O.C." for "Paid Outside of Closing" (settlement) and cannot be included in computing totals. P.O.C. items must not be placed in the Borrower or Seller columns, but rather on the appropriate line next to the columns. The settlement agent must indicate whether P.O.C. items are paid for by the Borrower, Seller, or some other party by marking the items paid for by whoever made the payment as "P.O.C. (payor)."

In the case of "no cost" loans where "no cost" encompasses third party fees as well as the up-front payment to the loan originator, the third party services to be paid for out of the adjusted origination charge must be itemized and listed on the HUD–1/1A with the charge for the third party service. These itemized charges must be recorded in the columns.

For charges disclosed using average cost pricing, the amount stated on the HUD–1 Settlement Statement as a charge to the borrower or seller for the settlement service must be the average price established pursuant to 24 CFR 3500.8(e).

* * * * *

Line Item Instructions

Section L. Settlement Charges

For all items except for those paid to and retained by the loan originator, the name of the person or firm ultimately receiving the payment must be shown. In the case of loans where third party settlement services, other than origination services, are paid from the adjusted origination charge by the loan originator, the individual third party settlement services should be itemized, with the charges shown in the columns. In those cases, the adjusted origination charge in line 803 will be a negative number large enough to offset the amounts of the third party settlement services that are paid out of the adjusted origination charge.

* * * * *

Line 801 is used to record "Our Service Charge," which is received by the loan originators. This number must not be listed in either the buyer's or seller's column.

Line 802 is used to record "Your charge or credit for the specific interest rate chosen," which states the charge or credit adjustment as applied to "Our Service Charge," if applicable. This number must not be listed in either column or shown on page one of the HUD–1.

Line 803 is used to record "Your Adjusted Origination Charges," which states the net amount of the loan origination charges. This number must be listed in either the buyer's column or as "paid outside closing."

Lines 804–811 may be used to record each of the "Required services that we select". Each settlement service provider must be identified by name and the amount paid recorded inside the columns or "P.O.C.".

Lines 808–811 may also be used to record other required lender or loan program disclosures. In such a case, any charge must be listed outside the columns.

* * * * *

Lines 1000–1009. * * *

After itemizing individual deposits in the 1000 series, the servicer shall make an adjustment based on aggregate accounting. This adjustment equals the difference between the deposit required under aggregate accounting and the sum of the itemized deposits. The computation steps for aggregate accounting are set out in § 3500.17(d). The adjustment will always be a negative number or zero (-0-). The settlement agent shall enter the aggregate adjustment amount on a final line of the 1000 series of the HUD–1 or HUD–1A statement.

Lines 1100–1115. This series covers title charges and charges by attorneys. The title charges include a variety of services performed by title companies or others, and include fees directly related to the transfer of title (title examination, title search, document preparation) and fees for title insurance. The legal charges include fees for Lender's, Seller's, or Buyer's attorney, or the attorney preparing title work. The series also includes any settlement, notary, or delivery fees.

Line 1101 is used to record the total for the category of "Title services and lender's title insurance," and the amount must be listed in the columns.

Lines 1102–1108 may be used to itemize charges paid other than those defined as "primary title services," such as for a closing attorney or escrow agent, and those charges paid must be listed outside the columns. Lines 1102–1108 may also be used to itemize some required title services whose costs are already included in Line 1101. In such a

case, any charge must be listed outside the columns.

Line 1109 is used to record "Lender's title insurance premium," and the amount must be listed outside the columns.

Line 1110 is used to record "Optional owner's title insurance," and the amount must be listed in the columns.

Line 1111 is used to record the lender's title insurance policy limits of coverage, and the amount must be listed outside the columns.

Line 1112 is used to record the owner's title insurance policy limits of coverage, and the amount must be listed outside the columns.

Line 1113 is used to record the title agent's portion of the total title insurance premium, and the amount must be listed outside the columns.

Line 1114 is used to record the underwriter's portion of the title insurance premium, and the amount must be listed outside the columns.

Line 1201 is used to record the total "Government recording and transfer charges," and the amount must be listed in the columns.

Lines 1202–1205 may be used to record specific itemized third party charges for government recording and transfer services, but the amounts must be listed outside the columns.

Lines 1301–1305 may be used to record additional itemized settlement charges, and the amounts must be listed in either column.

Line 1400 must state the total settlement charges stated within each column.

Line Item Instructions for Completing HUD–1A

Note: The HUD–1A, including the closing script addendum, is an optional form that may be used for refinancing and subordinate lien federally related mortgage loans, as well as for any other one-party transaction that does not involve the transfer of title to residential real property.[34] * * *

* * * * *

General Instructions for Completing Closing Script Addendum to HUD–1/1A Settlement Form

The settlement agent must complete the closing script addendum to the HUD–1/1A settlement form pursuant to § 3500.8(d) and in accordance with the instructions and example closing script forms contained in this Appendix A.

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[34] Note the HUD–1A and its instructions will be conformed to changes to the HUD–1 and HUD–1 instructions at the final rule stage.

OMB No. xxxx-xxxx
Approval Expires mm/dd/yyyy

Good Faith Estimate (GFE)

Name of Originator		Borrower	
Originator Address		Property Address	
Originator Phone Number			
Originator email		Date of GFE	

Instructions

This GFE gives you an estimate of your settlement charges and loan terms if you are approved for this loan. See page 3 for more detailed instructions.

Important dates

1. The interest rate for this GFE is available until . After that date, the interest rate, some of your Loan Origination Charges, and the monthly payment shown below can change until you lock your interest rate.
2. This estimate for all other settlement charges is available until .
3. If you proceed with this loan, you must go to settlement in days. You must lock the interest rate at least days before settlement.

Summary of your loan terms

Your Loan Details	
Your initial loan balance is	$
Your loan term is	years
Your initial interest rate is	%
Your initial monthly amount owed for principal, interest, and any mortgage insurance is	$ per month
Your rate lock period is *After you lock in your interest rate, you must go to settlement within this number of days to guarantee this interest rate.*	days
Can your interest rate rise?	☐ No ☐ Yes, it can rise to a maximum of %
Can your loan balance rise?	☐ No ☐ Yes, it can rise to a maximum of $
Can your monthly amount owed for principal, interest, and any mortgage insurance rise?	☐ No ☐ Yes, it can rise to a maximum of $
Does your loan have a prepayment penalty?	☐ No ☐ Yes, your maximum prepayment penalty is $
Does your loan have a balloon payment?	☐ No ☐ Yes, you have a balloon payment of $ due in years.
Does your loan include a monthly escrow payment for property taxes and, possibly, other obligations?	☐ No ☐ Yes

Summary of your settlement charges

A	Your Adjusted Origination Charges *(Table A, page 2)*	$
B	Your Charges for All Other Settlement Services *(Table B, page 2)*	$
A+B	**Total Estimated Settlement Charges**	$

Understanding your estimated settlement charges

Your Loan Details

1. Our service charge These charges are for the services we provide when we get and process this loan for you.	
2. Your credit or charge for the specific interest rate chosen (points) ☐ The credit or charge for the interest rate you have chosen is included in "Our service charge." (See item 1 above.) ☐ You receive a credit of $ for this interest rate of %. This credit reduces your upfront charges. ☐ You pay a charge of $ for this interest rate of %. This payment (discount points) increases your upfront charges. (See the table on page 3 to see how you can change this charge or credit by choosing a different interest rate.)	
A Your Adjusted Origination Charges	$

Your Charges for All Other Settlement Services

3. Required services that we select These charges are for services we require to complete your settlement. We will choose the providers of these services. *Service* / *Charge*	
4. Title services and lender's title insurance This charge includes the services of a title agent, for example, and title insurance to protect the lender, if required.	
5. Required services that you can shop for These charges are for other services that are required to complete your settlement. We can refer you to providers of these services or you can shop for them yourself. Our estimates for providing these services are below. *Service* / *Charge*	
6. Government recording and transfer charges This includes state and local charges on mortgages and home sales.	
7. Reserves or escrow This charge is held in an escrow account to pay recurring charges on your property, such as property taxes or insurance.	
8. Daily interest charges This charge is for the daily interest on your loan from the day of your settlement until the first day of the next month or the first day of your normal mortgage payment cycle. For this loan, this amount is $ per day for days (if your closing date is).	
9. Homeowner's insurance This charge is for the insurance you must buy for the property to protect from a loss, such as fire.	
10. Optional owner's title insurance This charge is for additional insurance you can choose to buy to protect yourself from title defects.	
B Your Charges for All Other Settlement Services	$
A + B Total Estimated Settlement Charges	$

Important Information and Instructions

Shopping for a loan offer

Only you can shop for the best loan for you. Compare this GFE with other loan offers, so you can find the best loan. Use the table on page 4 to compare all the offers you receive.

Understanding which charges can change at settlement

The GFE estimates your settlement charges. At your settlement, you will receive a HUD-1. Compare the charges on the HUD-1 with the charges on this GFE. Charges can change if you select your own provider and do not use the companies your lender suggests.

The list below shows you how much the estimated charges on this GFE can change at your closing.

These charges ***cannot increase*** at settlement:	The total of these charges ***can increase up to 10%*** at settlement:	These charges ***can change*** at settlement:
• Our service charge • Your charge or credit for the specific interest rate chosen *(after you lock in your interest rate)* • Government recording and transfer charges	• Required services that we select • Title services and lender's title insurance *(if we select them or you use providers identified by us)* • Required services that you can shop for *(if you use providers identified by us)* • Optional owner's title insurance *(if you use providers identified by us)*	• Required services that you can shop for *(if you do not use providers identified by us)* • Title services and lender's title insurance *(if you do not use providers identified by us)* • Reserves or escrow • Daily interest rate charges • Homeowner's insurance • Optional owner's title insurance *(if you do not use providers identified by us)*

Looking at trade-offs

In this GFE, we offered you a particular interest rate and estimated settlement charges. But, you could choose other loans to get a lower interest rate or lower settlement charges.

- If you want to choose a loan with a **lower interest rate,** then you will have **higher settlement charges.**
- If you want to choose a loan with **lower settlement charges,** then you will have a **higher interest rate.**

The table below shows how the loan for this GFE compares to two other options. If you decide you want to make one of these trade-offs, you must ask us for a new GFE.

	The loan in this GFE	A loan with a lower interest rate	A loan with lower settlement charges
Your loan amount	$	$	$
Your interest rate	%	%	%
How much your monthly payment will be	$	$	$
How much more or less in monthly payments from this GFE	No Change	You will pay $ less every month	You will pay $ more every month
How much more or less you will pay at settlement with this interest rate	No Change	Your lower interest rate will raise your settlement charges by $	Your higher interest rate will lower your settlement charges by $
How much your total estimated settlement charges will be	$	$	$

If this loan offer is for an adjustable rate loan, the comparisons in the table are for the initial interest rate before any adjustments are made.

Your financial responsibilities as a homeowner

In addition to your monthly amount owed for principal, interest, and mortgage insurance, you may need to pay other required annual charges to keep your property. We must provide an estimate for annual property taxes along with homeowner's, flood, and other required property protection insurance, but we are not required to provide estimates for the other charges. You may have to identify the other charges and ask for additional estimates from others.

Different sources might use different techniques to estimate these charges, but the actual charges will be the same in the end. Therefore, do not use these estimates to compare settlement charges from different loan originators.

Annual property taxes . . . .

Annual homeowner's insurance . . . .

Annual flood insurance . . . .

Annual homeowners association/condominium fees. . . .

Other . . . .

Total Other Annual Charges . . . .

Applying for this loan

If you decide you would like to apply for this loan, contact us at .
You must pay a fee of $. This fee will be subtracted from your settlement charges.

Getting more information

The type of loan you choose can affect your current and future monthly payments. You can ask us for more information about loan types. You can also look at several government publications: HUD's *Special Information Booklet* on settlement charges, your *Truth-in-Lending Disclosures*, and consumer information publications of the Federal Reserve Board.

Using the shopping chart

Use this chart to compare Good Faith Estimates (GFEs) from different loan originators. Fill in the information by using a different column for each GFE you receive.

By comparing loan offers, you can shop for the best loan.

	Loan 1	Loan 2	Loan 3	Loan 4
Loan Originator Name				
Initial Loan Balance				
Loan Term				
Initial Interest Rate				
Initial Monthly Amount Owed				
Rate Lock Period				
Can Interest Rate Rise?				
Can Loan Balance Rise?				
Can Monthly Amount Owed Rise?				
Prepayment Penalty?				
Balloon Payment?				
Total Estimated Settlement Charges				

If your loan is sold in the future

Lenders can receive additional fees by selling your loan at some future date after settlement. Once you have obtained your loan at settlement, however, your loan terms, adjusted origination charges, and total settlement charges cannot change. After settlement, any fees lenders receive in the future cannot change the loan you received or the charges you paid at settlement.

Homes & Communities U.S. Department of Housing and Urban Development

Sample Good Faith Estimate

As of May 1, 1996

Information by State

Print version

PART 3500 -- APPENDIX C

Appendix C to Part 3500 -- Sample Form of Good Faith Estimate

[Name of Lender]\1\

The information provided below reflects estimates of the charges which you are likely to incur at the settlement of your loan. The fees listed are estimates -- the actual charges may be more or less. Your transaction may not involve a fee for every item listed.

The numbers listed beside the estimates generally correspond to the numbered lines contained in the HUD - 1 or HUD - 1A settlement statement that you will be receiving at settlement. The HUD - 1 or HUD - 1A settlement statement will show you the actual cost for items paid at settlement.

Item\2\	HUD - 1 or HUD - 1A	Amount or range
Loan origination fee	801	$XXXX
Loan discount fee	802	$XXXX
Appraisal fee	803	$XXXX
Credit report	804	$XXXX
Inspection fee	805	$XXXX
Mortgage broker fee	[Use blank line in 800 Section]	$XXXX
CLO access fee	[Use blank line in 800 Section]	$XXXX
Tax related service fee	[Use blank line in 800 Section]	$XXXX
Interest for [X] days at $XXXX per day	901	$XXXX
Mortgage insurance premium	902	$XXXX
Hazard insurance premiums	903	$XXXX

Reserves	1000 - 1005	$XXXX
Settlement fee	1101	$XXXX
Abstract or title search	1102	$XXXX
Title examination	1103	$XXXX
Document preparation fee	1105	$XXXX
Attorney's fee	1107	$XXXX
Title insurance	1108	$XXXX
Recording fees	1201	$XXXX
City/County tax stamps	1202	$XXXX
State tax	1203	$XXXX
Survey	1301	$XXXX
Pest inspection	1302	$XXXX
[Other fees -- list here]		$XXXX

Applicant

Date

Authorized Official

These estimates are provided pursuant to the Real Estate Settlement Procedures Act of 1974, as amended (RESPA). Additional information can be found in the HUD Special Information Booklet, which is to be provided to you by your mortgage broker or lender, if your application is to purchase residential real property and the Lender will take a first lien on the property.

Footnotes

\1\The name of the lender shall be placed at the top of the form. Additional information identifying the loan application and property may appear at the bottom of the form or on a separate page. Exception: If the disclosure is being made by a mortgage broker who is not an exclusive agent of the lender, the lender's name will not appear at the top of the form, but the following legend must appear:

This Good Faith Estimate is being provided by XXXXXXXX, a mortgage broker, and no lender has yet been obtained.

\2\Items for which there is estimated to be no charge to the borrower are not required to be listed. Any additional items for which there is estimated to be a charge to the borrower shall be listed if required on the HUD - 1.

[58 FR 17165, Apr. 1, 1993, as amended at 59 FR 6521, Feb. 10, 1994]

U.S. Department of Housing and Urban Development
451 7th Street, S.W., Washington, DC 20410
Telephone: (202) 708-1112 Find the address of a HUD office near you

BARNEY FRANK, MA, CHAIRMAN

United States House of Representatives
Committee on Financial Services
2129 Rayburn House Office Building
Washington, DC 20515

SPENCER BACHUS, AL, RANKING MEMBER

June 12, 2008

The Honorable Steve Preston
Secretary
U.S. Department of Housing and Urban Development
451 7th Street, SW
Washington, DC 20410

Dear Mr. Secretary:

I am pleased that HUD is attempting to simplify and improve disclosure requirements under the Real Estate Settlement Procedures Act of 1974 (RESPA). The following are my comments on the proposed rule HUD published March 14, 2008.

Before final rule publication, HUD must work with the Federal Reserve Board to reconcile inconsistencies between the proposed RESPA and Truth in Lending Act (TILA) disclosure requirements to avoid consumer confusion and redundant disclosures. For example, HUD proposes loan term disclosures on the Good Faith Estimate (GFE) that duplicate or conflict with existing TILA requirements, such as requiring disclosure of the initial interest rate rather than the annual percentage rate as TILA necessitates. Also, proposed RESPA and TILA treatment of mortgage broker compensation disclosure differs substantially. Such discrepancies between RESPA and TILA not only serve to confuse consumers and frustrate industry but also undermine efforts to streamline and harmonize RESPA and TILA rules under the Economic Growth and Regulatory Paperwork Reduction Act of 1996.

HUD's proposed GFE disclosure of loan rates should include the annual percentage rate, which is more valuable to a consumer because it measures the true cost of the loan and facilitates comparison shopping. HUD proposed disclosure of mortgage broker compensation should be more aligned with the Board's approach, which requires an actual agreement between the consumer and the broker on maximum total broker compensation for high-cost loans.

HUD's requirements of the inclusion of an interest rate-based payment from a lender to a mortgage broker (i.e., a yield spread premium) in the calculation of the mortgage broker's total charges and disclosure of that payment on the GFE are significant RESPA improvements. However, I do not believe these additional disclosures fully address the harmful effects of such compensation. Interest rate-based payments provide an incentive for a mortgage broker or loan originator to steer a borrower to a loan with terms that are less advantageous than one for which he or she could otherwise qualify. Accordingly, originators of subprime loans should be banned from receiving any incentive compensation—including a yield spread premium—that is based on or varies with loan terms other than the amount of principal. This prohibition

has bi-partisan support and is contained in the Mortgage Reform and Anti-Predatory Lending Act of 2007, H.R. 3915, which the House overwhelmingly passed last fall.

Finally, I support allowing a loan originator to disclose on the HUD–1 an average cost price in accordance with HUD-established methods and clarifying that it is permissible for settlement service providers to negotiate discounts for settlement services, so long as the borrower is not charged more than the discounted price. However, to increase transparency, the actual cost to the consumer should also be disclosed on the HUD-1.

BARNEY FRANK
Chairman

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

SANDRA F. BRAUNSTEIN
DIRECTOR
DIVISION OF CONSUMER
AND COMMUNITY AFFAIRS

June 13, 2008

Regulations Division
Office of the General Counsel
U.S. Department of Housing and Urban Development
451 Seventh Street, SW
Room 10276
Washington, DC 20410-0001

Re: Docket No. FR-5180-P-01, Real Estate Settlement Procedures Act (RESPA): Proposed Rule to Simplify and Improve the Process of Obtaining Mortgages and Reduce Consumer Settlement Costs, 73 Fed. Reg. 14030 (Mar. 14, 2008)

To Whom it May Concern:

I am writing to provide the comments of Federal Reserve Board (Board) staff on the Department of Housing and Urban Development's (HUD) proposed amendments to Regulation X, which implements the Real Estate Settlement Procedures Act (RESPA). HUD's proposed amendments seek to simplify and improve the effectiveness of RESPA's disclosure of mortgage settlement costs so that consumers can make informed shopping decisions and avoid unnecessarily high settlement costs. We support HUD's goals and commend HUD for its continued efforts in this area. We also support HUD's efforts to consumer test the proposed RESPA disclosures. We look forward to working with HUD's staff to ensure that any changes to the RESPA rules are coordinated with the Board's rules under the Truth in Lending Act (TILA).

Background

RESPA seeks to protect consumers from unnecessarily high real estate settlement costs by (1) providing them with information about the costs required to close a mortgage loan, and (2) prohibiting certain business practices. A good faith estimate (GFE) is provided shortly after loan application, containing an itemized estimate of the costs the consumer will pay at closing (such as fees for a survey, appraisal, credit report, title examination and insurance, discount points and mortgage broker fees). The settlement statement (the HUD-1) provided in connection with the closing shows the actual costs paid and amounts to be held in reserve accounts. RESPA is implemented by HUD's Regulation X.

TILA's purpose is "to assure a meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various credit terms available to him and avoid the

uninformed use of credit."[1] TILA promotes the informed use of credit through standardized disclosures that reflect the cost over the life of the loan and highlight certain credit terms. To aid consumers in understanding the total cost, TILA requires the disclosure of two key terms—the finance charge and the annual percentage rate (APR). The finance charge reflects the cost as a dollar amount and includes interest as well as other costs such as origination fees, discount points, mortgage broker fees, and private mortgage insurance. The APR for closed-end mortgage loans is the total finance charge for the loan expressed as an annualized rate. Creditors must also provide a payment schedule showing the amount and timing of the consumer's payments, including any balloon payment, and specify whether any prepayment penalty may be imposed. TILA is implemented by the Board's Regulation Z.

Although RESPA's purpose is to inform consumers about settlement costs, and TILA's is to inform consumers about loan terms, these purposes overlap. Settlement costs may include loan origination fees, and consumers may finance their settlement costs. In 1996, Congress directed HUD and the Board to consider ways to harmonize the two rules and, if possible, combine the TILA and RESPA disclosures on a single form. In 1998, the agencies concluded that using a single disclosure form would benefit consumers and issued a joint report to Congress that included a prototype form developed for this purpose with the assistance of consumer focus groups.[2] The joint report also included recommendations for legislative reform.

Discussion

1. The agencies should develop, consumer test, and adopt a single form that complies with both RESPA and TILA.

Board staff believes that the agencies should continue to pursue ways to harmonize TILA and RESPA consistent with the Congressional mandate. A single, integrated form, which creditors may use to satisfy the requirements of both laws, would mitigate the problem of "information overload," and ensure that consumers review and understand the most important terms of the transaction. HUD's proposal, however, departs from the approach of a single, integrated disclosure form with little rationale, stating that "the proposed GFE is designed as a distinct, required form to promote shopping by consumers. HUD believes it is best complemented by providing a separate TILA disclosure along with the GFE."[3] HUD's approach would add more disclosures to the RESPA form, some of which would duplicate the disclosures required by TILA. As discussed below, our consumer testing for other disclosures has shown that "more" is not necessarily better or more meaningful and can, in fact, defeat the purpose of the disclosure. As discussed below, we are concerned that the contents of the two forms are duplicative and in some instances inconsistent. We urge HUD to coordinate its proposal with the Board to ensure that consumers receive information on loan terms and settlement costs on a single form at the same time.

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[1] 15 U.S.C. § 1601(a).

[2] *See generally* Joint Report to the Congress Concerning Reform to the Truth in Lending Act and the Real Estate Settlement Procedures Act (July 1998).

[3] 73 FR 14030, 14037 (March 14, 2008).

The Board's review of mortgage loan disclosures is already underway. The Board's goal is to make loan disclosures more effective and we will be reviewing the content and format of the disclosures, as well as their timing. The Board has begun conducting preliminary consumer testing for the mortgage disclosures currently required by TILA, as well as additional or different disclosures the Board may propose for comment. Our recent experience in testing credit card disclosures demonstrates the significant benefits of rigorous consumer testing that includes one-on-one cognitive testing of how consumers actually use the disclosures. Consumer testing provides valuable input about what information consumers understand and use, whether different terminology can enhance the disclosures' effectiveness, and how format changes can make the disclosures easier to navigate. Testing would also be instructive on the best way to combine the TILA and RESPA disclosures on a single form.

The Board recently proposed amendments to its TILA rules that would facilitate the creation of a single, combined TILA RESPA form consistent with the Congressional mandate. On December 18, 2007, the Board approved proposed amendments to Regulation Z, which would require creditors to provide TILA disclosures earlier to ensure that consumers receive them when they are most useful. Currently, creditors must provide TILA's cost disclosures within three days of receiving a written application for a home-purchase loan; for non-purchase mortgage loans, however, existing rules allow creditors to provide TILA disclosures anytime before the transaction is consummated. Under the Board's proposal, for <u>all</u> mortgage loans creditors would be required to provide the early TILA disclosure within three days after receiving a written application and before a fee is imposed (except a fee for obtaining a credit report). Accordingly, under the proposal creditors would provide TILA disclosures at the same time that they provide the GFE under RESPA. We suggest that any changes to the TILA and RESPA rules be coordinated to ensure creditors provide disclosures under both statutes at the same time.

HUD's proposal would permit lenders to charge consumers the cost of providing the GFE, which may include, but is not limited to, the cost of an initial credit report. The Board's rules would only permit a credit report fee before the early TILA disclosure is given to the consumer. The "cost of providing the GFE" is not defined in HUD's proposed rule. The rule should be revised to ensure that the fee is not substantial enough to discourage consumers from shopping and comparing different loan offers.

2. HUD's revised GFE, which would include details about loan terms, would be duplicative of and, in some cases, inconsistent with the TILA disclosures.

HUD's proposal would result in consumers receiving a disclosure distinct from TILA that duplicates details about loan terms. In some cases, the information on the revised GFE would overlap with the TILA disclosures, raising concerns about information overload. Our testing of credit cards and loan terms shows that providing too much information can lead consumers to disregard key information and focus instead on less significant features or terms. More importantly, the revised GFE provides information that seems inconsistent with the TILA disclosures, raising concerns about consumer confusion.

For example, the revised GFE would disclose the loan amount, while the TILA form would disclose the often-different "amount financed." The revised GFE would disclose a monthly payment that includes principal, interest, and mortgage insurance, but not property taxes and homeowner's insurance. Our preliminary testing of mortgage disclosures indicates that consumers find the monthly payment of "PITI" (principal, interest, taxes and insurance), to be the most useful measure of monthly cost. TILA permits creditors to include taxes and insurance in the monthly payment disclosure. In the case of adjustable rate mortgages (ARMs), the revised GFE would disclose the initial monthly payment and the maximum payment, without reference to when the maximum payment will go into effect, which may occur many years after. In contrast, TILA discloses the entire payment stream, using the rate or index then in effect.

In addition, the revised GFE would disclose the "initial interest rate" for an adjustable rate mortgation (ARM) while the TILA form would disclose the annual percentage rate (APR), which is based on interest at the fully-indexed rate and other finance charges. The initial interest rate often can be a temporary introductory rate and not the fully indexed rate then in effect. Focusing on the temporary rate may not be beneficial to consumers' understanding of the transaction, especially if the consumer does not know when or how much the rate can increase. The revised GFE also would show the maximum interest rate or "cap," but without knowing how quickly the interest rate can reach the cap, consumers could mistakenly believe that two loans with the same rate cap are identical. The Board's testing will look at how to present information about ARMs so that consumers can use it to shop and compare loans.

HUD proposes to address any confusion between the TILA disclosure and the RESPA GFE forms in a third disclosure, the Special Information Booklet given to consumers.[4] Given the Board's experience in consumer testing credit card and other disclosures, we believe it is unlikely that most consumers will take the time to navigate between the GFE and TILA disclosure on the one hand and the Special Information Booklet on the other in an effort to understand inconsistent loan terms. We believe that the inconsistencies and other differences between the proposed GFE and the TILA disclosure are likely to confuse consumers and, undermine consumers' ability to make informed shopping decisions and avoid unnecessarily high settlement costs.

3. Additional testing of the content and format of the proposed RESPA disclosures will enhance their effectiveness.

Board staff commends HUD for engaging in consumer testing. However, while the Board did not participate in HUD's testing of its revised GFE form, it does not appear that HUD's testing focused on how consumers understood the specific terms being disclosed on the revised GFE or whether they understood the multiplicity of terms represented in the different loan choices in the side-by-side comparison. A Federal Trade Commission study of mortgage disclosures was conducted after HUD's testing[5] and produced many new lessons and insights, which do not seem to have been incorporated in the revised GFE. Accordingly, the staff believes

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[4] 73 FR 14030, 14037 (Mar. 14, 2008).

[5] *See generally* "Improving Consumer Mortgage Disclosures: An Empirical Assessment of Current and Prototype Disclosure Forms, a Bureau of Economics Staff Report (June 2007).

that, notwithstanding HUD's consumer testing efforts, additional work is needed to test and develop a better disclosure.

Regarding disclosure of mortgage broker compensation, Board staff is concerned about consumers' understanding of the terminology used on the GFE. The revised GFE refers to yield spread premiums as the consumer's "credit" for the interest rate chosen, rather than broker compensation. The Board has proposed a different approach and is engaging in consumer testing. Clearly, consumers would benefit from consistent methodology and terminology in the disclosure of mortgage broker compensation. The Board's preliminary testing suggests consumers are confused about the broker's role in the transaction, e.g., whose interests the broker serves, who compensates the broker, and how the broker's compensation may affect a loan's interest rate or other terms. Board staff is concerned that the language on the revised GFE will contribute to consumer confusion rather than provide further clarity for consumers.

HUD is also proposing to require a "script" for closing agents to follow as they conduct the settlement. Board staff commends HUD for considering this novel approach, but we believe that consumer testing is needed to ensure that borrowers benefit from having the transaction explained in the precise manner dictated by HUD's script. We note that there may be practical difficulties with the script, including how closing agents would comply if the circumstances of a particular loan were not consistent with the HUD script.

Any effort to hasten adoption of new mortgage loan disclosures without adequate testing and development could, in the long run, hurt consumers more than help them, especially if consumers receive inconsistent disclosures under different legal regimes. The best interests of consumers can be served by an integrated approach to disclosing loan terms. We stand ready to work with HUD on this important effort.

Sincerely,

Sandra F. Braunstein

cc: Gary M. Cunningham
Paul S. Ceja

Congress of the United States
Washington, DC 20515

August 7, 2008

The Honorable Steven Preston
Secretary
U.S. Department of Housing and Urban Development
451 7th Street, S.W.
Washington, DC 20410

Dear Secretary Preston:

We appreciate your efforts to simplify and improve disclosures under the Real Estate Settlement Procedures Act (RESPA) and the Department of Housing and Urban Development's (HUD) recent decision to extend by an additional 30 days the public comment period for its proposed RESPA rule. However, this extension was not sufficient to address the concerns that we and the public have regarding the proposed rule's complexity, contentious provisions, incongruity with related federal agency efforts, and potential costs to consumers.

In light of these concerns, we request that HUD withdraw its proposed RESPA rule and immediately commence a joint rulemaking process with the Federal Reserve Board (Board) to produce more simplified mortgage and real estate settlement cost disclosure forms. To expedite this process, we also ask that you discard the hundreds of pages of HUD's current proposed RESPA rule that have not previously been the subject of public comment and cover a number of subjects beyond disclosures.

The concept of a joint HUD-Board rulemaking is not new. In 1996, Congress requested that HUD and the Board collaborate on a joint RESPA-Truth in Lending Act (TILA) rule. In 1998, HUD and the Board issued a report to Congress confirming that the agencies should jointly produce mortgage disclosure forms. On June 13th, 2008, the Board sent a letter to HUD encouraging such a coordinated effort that includes adequate consumer testing and specifically requested that the two federal regulatory bodies avoid conflicts as they work to modernize disclosures required by RESPA and TILA.

In the July 1, 2008, issue of *American Banker*, Sandra Braunstein, the Board's Director of the Division of Consumer and Community Affairs, said:

> "Any effort to hasten adoption of new mortgage loan disclosures without adequate testing and development could, in the long run, hurt consumers more than help them, especially if consumers receive inconsistent disclosures under different legal regimes . . . A single, integrated form, which creditors may use to satisfy the requirements of both laws, would mitigate the problem of 'information overload'."

We couldn't agree more.

As HUD proceeds with RESPA reform in concert with the Board, we also encourage you to ensure that any final proposal focuses on disclosures and enjoys the consensus of industry and consumer groups. Following HUD's withdrawal of the last RESPA regulation in 2004, then-Secretary Jackson told the National Association of Realtors Midyear Legislative Meetings & Trade Expo:

> "If you want a bill [regulation] you have to have consensus . . . Therefore, next time we will sit at a table, as we did at negotiated rulemaking. We will talk with the groups. If we have 75 percent or 80 percent agreement we will have a bill [regulation]."

2

Unfortunately, HUD's current RESPA proposal does not reflect this consensus. And, again, RESPA stakeholders have not previously vetted -- nor reached any agreement on -- numerous provisions within HUD's proposed RESPA rule. We encourage you to honor HUD's commitment and work with stakeholders to promulgate a new rule that receives broad support.

Finally, we ask that you work to produce a RESPA rule that takes into consideration its impact on small businesses and especially consumers. The current proposal, which to our knowledge has not undergone extensive consumer testing, promises to be more confusing and costly to both small businesses and consumers.

On June 11, 2008, Small Business Administration (SBA) Chief Counsel for Advocacy Thomas Sullivan and Assistant Chief Counsel for Economic Regulation and Banking Jennifer Smith sent a letter to HUD Assistant Secretary for Housing-Federal Housing Commissioner Brian Montgomery expressing "concerns with the potential economic impact of the proposal" on small businesses.

Given these concerns and the thousands of others raised by our constituents and industry stakeholders, we are profoundly concerned that HUD's proposed RESPA rule will hinder rather than help the recovery of the housing market. It is critically important for consumers that any revision to RESPA achieve the following goals: simplify, clarify, and reduce the cost of the mortgage and real estate settlement processes.

For these reasons, it is vital that HUD take a new and important step toward positive reform by immediately withdrawing its current proposal and, working with the Board, embark on a joint rulemaking process to improve RESPA and TILA disclosures.

Sincerely,

Rubén Hinojosa
Member of Congress

Judy Biggert
Member of Congress

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Greg Walden	Gene Green
Jim Matheson	Lynn Westmoreland
Robert Aderholt	Randy Kuhl
Eddie Bernice Johnson	Jan Schakowsky
John Boozman	[illegible]
Lee Terry	[illegible]
Gus M. Bilirakis	McCotter
[illegible]	[illegible]
John Campbell	[illegible]
Joe Donnelly	Dean Heller
Loretta Sanchez	Pete Sessions

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C.A. Dutch Ruppersberger	Donald M. Payne
Bill Delahunt	[illegible] IL-19
[illegible]	Sanford D. Bishop Jr.
Harold Rogers	[illegible]
Dave Hobson	[illegible]
[illegible]	Nita M. Lowey
Mark Souder	Lincoln Diaz-Balart
Rosa L. DeLauro	
[illegible]	

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Mary Bono Mack	Pat Tiberi
Ander Crenshaw	Connie Mack
Steve Chabot	Robin Hayes
Michael T. McCaul	Brian P. Bilbray
Charles A. Wilson	Patrick T. McHenry
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Rob A. Brady	Ron Paul
Charles A. Gonzalez	Mike Ross
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Stephanie Herseth Sandlin

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Kay Granger

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Wm. Lacy Clay

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Brian Higgins

Randy Neugebauer

John Culberson

Al Green

Thomas Price

Allyson Y. Schwartz

Bill Sali

7

Marsha Blackburn

Brad Ellsworth

Tim Murphy

8

[illegible]	Peter DeFazio
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Peter J. Visclosky	Ciro D. Rodriguez
Ed Pastor	Howard Coble
Ellen Tauscher	Dennis J. Kucinich
Tammy Baldwin	[illegible]
Gary G. Miller	Ralph M. Hall
Jerry F. Costello	Lamar Smith

9

[illegible]

T. Holden

Ron Lewis

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Dan Burton

Frank D. Lucas

Joe Knollenberg

Gregory W Meeks

Chet Edwards

[illegible]

Tom Latham

Ed Whitfield

[illegible]

Corrine Brown

Carolyn B Maloney

Terry Everett

Bill Foster

Travis W Childers

James T Walsh

[illegible]

Donald Manzullo

10

Jim Saxton

Steve Buyer

Jerry Moran

Jim Gibbons

John M. McHugh

11

Carolyn McCarthy	[illegible]
[illegible]	[illegible]
[illegible]	Joe Courtney
Baron P. Hill	Candice S. Miller
[illegible]	Jerry McNerney
[illegible]	[illegible]
Bill Shuster	Lois Capps
[illegible]	Steve Scalise
Thelma Drake	Mike Castle
[illegible]	[illegible]
[illegible]	Virgil Goode Jr.

Marilyn Musgrave 12

Steve King

Cathy McMorris Rodgers

[illegible]

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Jim Langevin	Charles W. Dent
Mike Thompson	[illegible]
Rodney Alexander	Tim Walberg
Ginny Brown-Waite	Madeleine Z. Bordallo
Gabrielle Giffords	Artur Davis
Joe Sestak	Sam Farr
Allen Boyd, Jr.	[illegible]
Jason Altmire	Zach Wamp
Neil Abercrombie	Stevan Pearce
Betty McCollum	Elijah E. Cummings
Chris Smith	[illegible]

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Todd Tiahrt

Louise M. Slaughter

Frank A. LoBiondo

15 Lucille Roybal-Allard

Chaka Fattah

[illegible]

Howard L. Berman

Bud Cramer

Russ Carnahan

Betty Sutton

Jeff Miller

Carol Shea-Porter

Leonard L. Boswell

John Kline

Shelley Moore Capito

Scott Garrett

Bobby Scott

Lynn A. Westmoreland

Phil Hare

Steven R. Rothman

Pat [illegible]

Eleanor Holmes Norton

Jim Oberstar

Nick Rahall

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[illegible]

Gary L. Ackerman

Tim Johnson

Yvette D. Clarke

[illegible]

Joe Wilson

Doris O. Matsui

Virginia Foxx

Sheila Jackson Lee

Michael McMahon

Joe Baca

Peter Welch

Eric Cantor

Keith Ellison

[illegible]

Darrell Issa

John Barrow

Mike Doyle

Marion Berry

Donna F. Edwards

Paul C. Broun

Mac Thornberry

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Marchant, Kenny	(R-TX)
Allen, Thomas H.	(D-ME)
Davis, Geoff	(R-KY)

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Matheson, Jim	(D-UT)
Aderholt, Robert B.	(R-AL)
Johnson, Eddie Bernice	(D-TX)
Boozman, John	(R-AR)
Terry, Lee	(R-NE)
Bilirakis, Gus M.	(R-FL)
Cleaver, Emanuel	(D-MO)
Campbell, John	(R-CA)
Donnelly, Joe	(D-IN)
Sanchez, Loretta	(D-CA)

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Delahunt, William D.	(D-MA)
Hinchey, Maurice D.	(D-NY)
Rogers, Harold	(R-KY)
Hobson, David L.	(R-OH)
Green, Gene	(D-TX)
Souder, Mark E.	(R-IN)
DeLauro, Rosa L.	(D-CT)
Ros-Lehtinen, Ileana	(R-FL)

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Bono Mack, Mary	(R-CA)
Crenshaw, Ander	(R-FL)
Chabot, Steve	(R-OH)
McCaul, Michael T.	(R-TX)
Wilson, Charles A.	(D-OH)
Bishop, Timothy H.	(D-NY)
Brady, Robert A.	(D-PA)
Gonzalez, Charles A.	(D-TX)
Bean, Melissa L.	(D-IL)
Pryce, Deborah	(R-OH)
Cazayoux Jr., Donald J.	(D-LA)

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Biggert, Judy	(R-IL)
Sires, Albio	(D-NJ)
Shays, Christopher	(R-CT)
Moore, Gwen	(D-WI)

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Tanner, John S.	(D-TN)
LaHood, Ray	(R-IL)
Kuhl Jr., John R. "Randy"	(R-NY)
Loebsack, David	(D-IA)
McCarthy, Kevin	(R-CA)
Mahoney, Tim	(D-FL)
McCotter, Thaddeus G.	(R-MI)
Moore, Dennis	(D-KS)
Putnam, Adam H.	(R-FL)
Heller, Dean	(R-NV)
Sessions, Pete	(R-TX)

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Payne, Donald M.	(D-NJ)
Shimkus, John M.	(R-IL)
Bishop, Sanford D. Jr.	(D-GA)
Harman, Jane	(D-CA)
Wu, David	(D-OR)
Lowey, Nita M.	(D-NY)
Diaz-Balart, Lincoln	(R-FL)

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Tiberi, Patrick J.	(R-OH)
Mack, Connie	(R-FL)
Hayes, Robin	(R-NC)
Bilbray, Brian P.	(R-CA)
McHenry, Patrick T.	(R-NC)
Porter, Jon C.	(R-NV)
Paul, Ron	(R-TX)
Ross, Mike	(D-AR)
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U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-1000

ASSISTANT SECRETARY FOR CONGRESSIONAL
AND INTERGOVERNMENTAL RELATIONS

The Honorable Judy Biggert
U.S. House of Representatives
Washington, DC 20515-6050

Dear Representative Biggert:

On behalf of Secretary Preston, thank you for your letter of August 7, 2008, concerning the Department's efforts to simplify and improve disclosures under the Real Estate Settlement Procedures Act (RESPA). HUD is aware of the high level of interest in the proposed rule.

As you acknowledge in your letter, the Department extended its original 60 day public comment period to 90 days to assure meaningful public comment. During that process, the Department received extensive and thoughtful comments from individuals, members of Congress, consumer organizations, industry associations, and numerous companies involved in the loan origination and settlement process including lending institutions, mortgage brokers, real estate agents, attorneys, and title and settlement agents, as well as federal and state regulators. The Department continues to carefully consider these comments, and will make appropriate modifications and improvements to the rule.

The current housing finance situation has dramatically highlighted the need to move forward responsibly and expeditiously with measures to help American homebuyers. Many of the current difficulties, including the high rate of foreclosures, have been caused in part by consumers not fully understanding their loan terms and costs. The Department believes that a rule is needed to help consumers avoid such difficulties in the future.

The Department has been listening hard to all of the stakeholders in this process, and intends to strike a proper balance among their concerns. This includes concerns raised by members of Congress, the different industry groups, consumers, and governmental entities. As Secretary Preston stated during his confirmation hearing, "it is important for individuals to understand what they are getting into. I am hopeful that can be done in a way that is not overly burdensome to the industry."

Thank you again for your comments regarding the rule. The Department looks forward to continuing to work with members of Congress and all other interested parties regarding its RESPA reform efforts. I would ask that you forward a copy of this response to the other signatories on your letter.

Sincerely,

Sheila M. Greenwood
Assistant Secretary for Congressional
and Intergovernmental Relations

Statement of the

Independent Community Bankers of America

For the Record
In the
Hearing on

"HUD's Proposed RESPA Rule"

Before the
Subcommittee on Oversight and Investigations
Committee on Financial Services
United States House of Representatives

September 16, 2008
Washington, D.C.

The Independent Community Bankers of America[1] (ICBA) welcomes the opportunity to share its views with members of the Subcommittee on Oversight and Investigations on the Department of Housing and Urban Development's Proposed Rule, "Real Estate Settlement Procedures Act (RESPA): To Simplify and Improve the Process of Obtaining Mortgages and Reduce Consumer Settlement Costs." ICBA strongly opposes the proposed regulation and filed a comment letter with HUD explaining our opposition.

ICBA opposes the proposed rule for the following reasons:

- **Burden on Community Banks.** The changes proposed by HUD will substantially change disclosures and elements of the mortgage transaction. Community banks and other small businesses would face significant burdens in implementing the changes due to changes in systems and forms and employee training. It would be far more difficult for community banks to absorb the costs as they have relatively low mortgage volume over which to spread the costs as compared to larger loan originators.
- **Proposal is Inconsistent with Other Regulations and Laws.** ICBA has serious concerns about the lack of consistency between this proposal and other laws and regulations, including the Truth in Lending Act, Home Ownership and Equity Protection Act, Home Mortgage Disclosure Act, Equal Credit Opportunity Act, and the Fair Credit Reporting Act. Lack of consistency among existing or proposed laws and regulations makes

[1] *The Independent Community Bankers of America represents nearly 5,000 community banks of all sizes and charter types throughout the United States and is dedicated exclusively to representing the interests of the community banking industry and the communities and customers we serve. ICBA aggregates the power of its members to provide a voice for community banking interests in Washington, resources to enhance community bank education and marketability, and profitability options to help community banks compete in an ever-changing marketplace.*
With nearly 5,000 members, representing more than 18,000 locations nationwide and employing over 268,000 Americans, ICBA members hold more than $908 billion in assets, $726 billion in deposits, and more than $619 billion in loans to consumers, small businesses and the agricultural community. For more information, visit ICBA's website at www.icba.org.

compliance difficult and information provided to the consumer very confusing. In addition, HUD has exceeded its authority in some instances.

- **New "Good Faith Estimate" Unlikely to Produce Benefits.** The new procedure to obtain a "good faith estimate" ("GFE") of loan costs will significantly increase the paperwork and process burden of lenders without any meaningful benefits for consumers.
- **Settlement Cost Tolerances Are Too Narrow and Do Not Reflect Realities in the Mortgage Process.** The settlement cost tolerances provided in the proposal are too narrow and limited. The tolerances are not flexible enough to reflect what can and does change outside the control of the lender. As a result, some smaller volume lenders, such as community banks may find it is no longer profitable to continue to offer residential mortgages, if they experience many costs that exceed tolerances.
- **Discounts and Average Cost Pricing Will Disadvantage Smaller Lenders and Settlement Cost Providers.** ICBA is concerned that the use of average cost pricing and volume based discounts unfairly disadvantages smaller lenders and small businesses that provide settlement services. . Large volume lenders could use average cost pricing to drive smaller lenders out of certain markets.
- **Closing Script is Not Workable.** The closing script is very long and complicated and is presented at a time in the transaction when borrowers and settlement agents are usually pressed for time. Since it will often be read by a settlement agent or person other than the lender, it may be difficult for borrowers to get adequate or accurate answers to any questions. Because of

the length of the script and time constraints, the intended benefits of the script may not often be realized.

- **Proposal is Ill-Timed.** HUD's proposal is ill-timed. The changes will cause significant disruptions to a mortgage industry already in turmoil.
- **HUD Needs Additional Authority to Enforce RESPA in Non-Bank Institutions.** ICBA supports providing additional authority to HUD to enable it to enforce settlement services laws and regulations in institutions that are not currently under the oversight of the banking agencies to ensure even enforcement across the mortgage industry.
- **Changes Could Increase Cost of Homeownership.** These changes do not reflect the realities of the mortgage market and industry, may cause more serious disruption, and may increase the cost of homeownership at a critical time when lenders and borrowers are endeavoring to work through many challenges.

A more detailed discussion of our concerns follows.

Summary of Proposed Regulation

The proposed rule is HUD's latest attempt to simplify and improve the disclosure requirements for mortgage settlement costs under RESPA. HUD intends its proposal to protect consumers from unnecessarily high settlement costs by improving and standardizing the Good Faith Estimate (GFE) form to make it easier to use for shopping among settlement service providers, to facilitate comparison of the GFE and the HUD-1/HUD-1A Settlement Statements, and to clarify HUD's current regulations concerning discounts and expressly state when RESPA permits certain pricing mechanisms that benefit consumers including

average cost pricing and discounts, including volume based discounts, among other provisions.

ICBA Supports Easy to Understand Disclosures. ICBA has long supported mortgage disclosures that are simple and easy to understand, clearly specifying the obligations and responsibilities of all parties. Disclosures should focus on the information consumers want most: the principal amount of the loan, the simple interest rate on the promissory note, and the amount of the monthly payment. They should be provided at the appropriate stage of a transaction to allow consumers to make informed decisions and to shop for the best mortgage for their situation.

Changes to Add Burden to a Mortgage Industry in Turmoil. The changes proposed by HUD are significant and will substantially change disclosures and elements of the mortgage transaction. They will cause significant disruptions to a mortgage industry already in turmoil. If HUD goes forward with the proposed rule, community banks and other small businesses will face significant burdens in implementing the changes due to changes in systems and forms and employee training. It will be far more difficult for community banks to absorb the costs as they have relatively low mortgage volume over which to spread the costs as compared to larger loan originators.

Need for Consistency Among Laws and Regulations

ICBA has serious concerns about the lack of consistency between this proposal and other laws and regulations. For example, requirements regarding when the lender must provide the consumer with a GFE rejection notice in the HUD proposal is inconsistent with the requirements of the Equal Credit Opportunity Act (ECOA) and the Fair Credit Reporting Act. Amendments to regulations implementing RESPA should be consistent with laws and regulations implementing the Truth in Lending Act, Home Ownership and Equity Protection

Act, Home Mortgage Disclosure Act, ECOA, and the Fair Credit Reporting Act. Lack of consistency among existing or proposed laws and regulations makes compliance difficult and information provided to the consumer very confusing.

HUD has Exceeded its Authority. In addition, ICBA is concerned that HUD has exceeded it authority in several instances in the rule. For example, RESPA is focused on effecting changes in the settlement process for residential real estate to provide more effective advance disclosure to home buyers and sellers of settlement costs, eliminate kickbacks or referral fees, reduce the amounts homebuyers are required to keep in escrow accounts and to reform and modernize the local recordkeeping of land title information. HUD is authorized by the statute to prescribe rules and regulations, make interpretations, and to grant reasonable exemptions for classes of transactions as necessary to accomplish this. Placing limitations on the amount closing costs may change before settlement or permitting the use of average cost pricing for settlement fees are not consistent with this charge. Nor, are these proposals consistent with RESPA's historic focus on making "good faith estimates" at the time of the application and disclosing the specific amount of a closing cost in the HUD-1.

We also question HUD's authority to require a notification to the borrower of the application's rejection when this is already required by ECOA, as discussed further below.

New "Good Faith Estimate" Unlikely to Produce Benefits

The new procedure to obtain a "good faith estimate" ("GFE") of loan costs will significantly increase paperwork and process burden of lenders without any meaningful benefits for consumers.

GFE to be Based on Limited Consumer Information. HUD proposes that potential borrowers be provided a new GFE Application form comprised of items of information that

the borrower would submit to receive a GFE. The proposed GFE Application would only contain the borrower's name, social security number, property address, gross monthly income, borrower's estimate of the house price, and the amount of loan sought. Such limited information, which does not include the listing of other assets or expenses, makes it difficult for the loan originator to get a true financial picture of the borrower. Yet, the loan originator would use this information to make an initial credit decision and provide the borrower a GFE.

Limited Fee Does Not Adequately Compensate Lender. The borrower can only be charged a limited fee for providing the GFE, including the cost of an initial credit report. No other fees, such as for an appraisal or inspections, can be collected before the GFE is provided. The GFE has been expanded from one page to four. Thus, the loan originator must complete significantly more work, while receiving a limited fee that does not completely compensate the originator for the work. This is particularly burdensome for smaller volume originators that may not have some of the automated systems used by large volume originators that provide cost efficiencies.

Borrower's Changes Would Necessitate Another GFE. In addition, HUD proposes more paperwork for the loan originator in the event that the borrower requests changes in the loan identified in the GFE, such as changes to settlement charges and terms of the loan. The originator must then notify the borrower within one day and treat it as a decision to reject the loan. A revised GFE must be provided, if another loan is available. Thus, a borrower could ask for information about an ARM versus a fixed rate loan, or slightly change the amount of the loan or the amount of points—all requiring a revised GFE. Before closing, borrowers with new homes under construction often make changes that necessitate changes to the loan and the generation of revised disclosures.

In today's real estate environment, sellers are often negotiating the payment of settlement and other costs late in the transaction in order to sell their home; again this

necessitates new disclosures. We do not see that this situation was foreseen in the development of proposed disclosures. Again, the result will be the provision of new disclosures, which will be more burdensome for smaller volume loan originators whose limited staff resources must generate this additional paperwork.

New Disclosures Could Confuse Borrowers. ICBA believes that the new disclosures will also confuse potential borrowers even more than the current disclosure scheme. The information on the new GFE will certainly change because it is given so early in the transaction, yet the borrower is led to believe that the costs listed on the form are fixed. In reality, many of these costs will likely change as the transaction moves forward due to decisions that the borrower makes or other factors that change as information is gathered about the property, the borrower and the loan. For example, borrowers often decide to change the principal amount of the loan, which in turn can cause other settlement charges to change.

Inconsistencies with HUD-1. Also, there remains a great deal of difference between the GFE and the HUD-1/HUD-A. To gain the benefits in comparing the documents that HUD intends, significantly more work needs to be done. However, as discussed further below, we do not think that now is the right time to embark on such radical changes to the mortgage industry.

One-Day Notice is Burdensome. ICBA is also concerned with the requirement to notify the consumer within one day of the decision to reject the loan. First, this is an extremely tight deadline that will likely be difficult for originators to meet, particularly if they have limited staff resources. It is also a much shorter timeframe than provided for notices required by other credit regulations. The notice is also duplicative. ECOA already requires that creditors provide notice of denial within 30 days of the application and provide reasons for the adverse action.

Settlement Cost Tolerances Are Too Narrow and Do Not Reflect Realities in the Mortgage Process

The proposal would prohibit charges of loan originators at settlement from exceeding the amount listed as "our service charge" on the GFE, absent unforeseeable circumstances. Originator-required services where the originator selects the third party provider and originator-required services where the borrower selects from a list of third party providers identified by the originator, among other items, could not increase more than 10 percent at closing from the amount disclosed on the GFE, absent unforeseeable circumstances.

Costs Locked in Too Early. First, ICBA objects to HUD using tolerances in an effort to lock costs in so early in the transaction. ICBA is very concerned that these tolerances are too narrow and limited. What HUD sees as "unforeseeable circumstances" is not flexible enough to reflect what can and does change, outside the control of the lender, in many mortgage transactions between the time the GFE is provided and settlement.

Unforeseen Costs Could Not Be Passed Along. For example, it appears that an originator could not pass along to the borrower increases in government recording and transfer charges that it has no control of, or the cost of additional work needed on an appraisal or survey due to characteristics of the property (though the cost of a second appraisal is allowed). It will be far more difficult for smaller loan originators to absorb variances in these costs that cannot be passed on to borrowers due to their lower volume of loans (and thus income) as compared to that of larger volume market participants.

Some Small Lenders Might Cease Mortgage Lending. The rule would provide the originator with the ability to provide new disclosures to the borrowers when costs rise due to unforeseen circumstances (defined in the proposal), but this may be costly and burdensome to the originator. As a result, some smaller volume lenders, such as community banks may find

it is no longer profitable to continue to offer residential mortgages, if they experience many cost that exceed tolerances. They may exit the market, thereby reducing competition and consumer choice.

Discounts and Average Cost Pricing Will Disadvantage Smaller Lenders and Settlement Cost Providers

The proposal intends to clarify HUD's current regulations concerning discounts and expressly state when RESPA permits certain pricing mechanisms that benefit consumers, including average cost pricing and discounts, including volume based discounts, for settlement services. ICBA is concerned that the use of average cost pricing and volume based discounts unfairly disadvantages smaller lenders and small businesses that provide settlement services.

Larger market participants have a greater ability to negotiate volume discounts for services needed in the settlement process than do smaller participants because of their size. ICBA remains concerned about the ability of smaller lenders and settlement service providers to compete against larger participants.

ICBA is also concerned as to how average cost pricing would be viewed during an examination process since HUD provides little guidance on how such pricing would be determined. Institutions with smaller mortgage volume could be examined relatively easily as compared to large volume institutions. A great deal of unfair competitive pricing can be hidden in high volume averages, making it difficult for smaller volume institutions to compete. Large volume lenders could use average cost pricing to drive smaller lenders out of certain markets. While consumers may benefit by lower costs in the short run, they would be hurt over the long run by fewer credit options and the potential for monopolistic control of a local market.

Closing Script Is Not Workable

ICBA has strong concerns about the workability of the proposed closing script that is to be read at closing and signed by the borrower. HUD proposes an addendum to the HUD-1 that is prepared by the settlement agent based on information provided by the loan originator that reflects the loan documents and settlement information. The addendum would compare loan terms and settlement charges estimated on the GFE with those on the HUD-1 and would describe in detail the loan terms for the specific mortgage loan as stated in the mortgage note and related settlement information.

The closing script is intended to act as a final check to ensure that the borrower truly understands the terms of the loan he or she has agreed to has merit. However, we do not think that the proposed closing script is workable. First, it is very long and complicated and is presented at a time in the transaction when borrowers and settlement agents are usually pressed for time. Second, since it will often be read by a settlement agent or person other than the lender, it may be difficult for borrowers to get adequate or accurate answers to any questions. Because of the length of the script and time constraints, the intended benefits of the script may not often be realized.

The Proposal is Ill-Timed and Could Exacerbate Turmoil in the Mortgage Markets

While clearly there is a need to make appropriate changes to any parts of the mortgage lending business that are broken, we have serious concerns about implementing such broad changes during a time when lenders are working to help troubled borrowers restructure their loans so they can remain in their homes.

Other Significant Changes Occurring. Significant changes are occurring in the Federal Housing Administration and other lending programs intended to address the problems in the mortgage industry. Many community banks have responded positively to

these changes and are learning about the programs so they can offer them to consumers in their communities. Community banks were not generally participants in subprime lending and did not engage in the irresponsible lending practices that placed borrowers in mortgages inappropriate for their financial situation. However, community banks are stepping forward to assist these borrowers when able and are working to provide mortgages when other lenders have stepped aside.

If HUD goes forward with the proposed rule, community banks and other small businesses will face significant costs and burdens in implementing the changes due to changes in systems and forms and training. It will be more difficult for community banks to absorb the costs as they have relatively low mortgage volume to spread the costs over as compared to larger loan originators.

HUD Itself Estimates High-Cost for Changes for Community Banks. HUD's own analysis in Appendix II.C.3. *Savings and Transfers, Efficiencies, and Costs* notes that total one-time compliance costs to the lending and settlement industry of the proposed GFE and HUD-1 predominately will fall on small business ($390 million or 68% of an estimated $570 million to the industry). We have serious concerns about the ability of community banks with limited staff resources to implement such broad RESPA changes concurrently with learning new loan programs and reaching out to help troubled borrowers, functions so important to getting our country out of the current mortgage credit crisis. In our view, it is the wrong time to make such drastic changes to the mortgage lending process.

HUD Needs Additional Authority to Enforce RESPA in Non-Bank Institutions

ICBA has long held that existing laws and regulations should be enforced against predatory lenders before new laws and regulations are sought. Currently, insured depository institutions are the only entities regularly examined for compliance with existing laws and

regulations established to protect borrowers. The ICBA supports one set of rules for all mortgage lenders, and regulation, supervision and enforcement must be consistent across the industry. For banks, this should be carried out by their primary regulator. ICBA supports providing additional authority to HUD to enable it to enforce settlement services laws and regulations in institutions that are not currently under the oversight of the banking agencies to ensure even enforcement across the mortgage industry.

Summary

Consumers need adequate and appropriate disclosure about the terms and costs of mortgages to enable them to understand the transaction and facilitate shopping for the best mortgage for their situation. HUD has proposed amendments to its RESPA rules that significantly and substantially change mortgage disclosures and elements of the mortgage transaction. These changes do not reflect the realities of the mortgage market and industry, may cause more serious disruption, and may increase the cost of homeownership at a critical time when lenders and borrowers are endeavoring to work through many challenges.

THE NATIONAL CREDIT REPORTING ASSOCIATION, INC.

September 16, 2008

Hon. Melvin L. Watt, Chairman
Subcommittee on Oversight & Investigations
Committee on Financial Services
2236 Rayburn House Office Building
Washington, DC 20515

Dear Mr. Watt: .

Thank you for holding today's hearing on the Department of Housing & Urban Development's (HUD) proposed changes to the Real Estate Settlement Procedures Act (RESPA). On behalf of the National Credit Reporting Association (NCRA), I am writing to submit comments NCRA has made to HUD for inclusion in the hearing record.

NCRA is a national trade organization of independent credit reporting agencies that specialize in consumer mortgage credit reports. NCRA members compile consumer credit data from the three national repositories and work with consumers to ensure that lenders see their most complete—and accurate—credit history possible. Thus, NCRA members are frequently able to help consumers save thousands of dollars in mortgage payments.

The attached document expresses our concern that HUD's proposal could limit the consumer and lender's choice of credit products, unfairly exposing consumers to higher interest rates, and offers our suggestions for more effective ways to achieve HUD's goals. Thank you for your attention to this issue, and for your consideration of these comments.

Sincerely,
Terry Clemans
Executive Director

NATIONAL CREDIT REPORTING ASSOCIATION, INC
Comments on HUD's Proposed RESPA Rule -Docket No. FR-5180-P-01

September 16, 2008

Comments on the
Department of Housing and Urban Development
24 CFR Parts 203 and 3500

Real Estate Settlement Procedures Act (RESPA):
Proposed Rule to Simplify and Improve the Process of
Obtaining Mortgages and Reduce Consumer Settlement Costs; Proposed Rule

Re: Docket No. FR-5180-P-01

The National Credit Reporting Association, Inc. (NCRA) would like to provide the Department of Housing and Urban Development (HUD) comments regarding what it perceives to be problems with HUD's Real Estate Settlement Procedures Act (RESPA): Proposed Rule to Simplify and Improve the Process of Obtaining Mortgages and Reduce Consumer Settlement Costs; Proposed Rule, 24 CFR Parts 203 and 3500.

NCRA would like to thank HUD for its efforts in resolving the problems with RESPA. We recognize the great need for reform as the current law is impossible to enforce uniformly on a national basis due to various Appellate court rulings. We also see on a daily basis both as consumers ourselves when buying a home, and as industry partners many abuses to the current RESPA rule. Consumers are often shocked at the closing table and the numbers between the GFE and the HUD-1 are rarely consistent. While reform is needed, HUD must be very careful to not create new areas of abuse, and cause more harm than it solves via the reform.

HUD's proposed RESPA rule covers numerous aspects of the settlement service process. While NCRA understands HUD's desire to reform RESPA and appreciates the efforts HUD has taken in evaluation of the process, we urge HUD to not move forward with the proposed rule as it falls short of addressing the issues. NCRA believes that if HUD does choose to go forward with this proposed rule, many consumers will find that the rule creates larger barriers to home ownership and an increases of costs, the exact opposite of HUD's stated intentions for the reform.

NCRA will only address the segments of the proposed rule that specifically relate to the credit report used in the mortgage process. While one of the lowest cost individual items[1] in the products and services categorized by HUD as "Settlement" services of a mortgage loan, the credit report is one of the most important, as it alone is the primary element in setting the highest cost item of the mortgage loan, the cost of the interest on the loan itself.[2]

[1] Federal Register /Vol.73, No.51/Friday, March 14, 2008/Proposed Rules pages 14076, 14079, 14082, 14085, 14088, 14091. These are examples of closing costs used by HUD in the proposed rule. In each example the credit report ranged from a low of $18.00 and a high of $45.00 with only the Flood certification being lower in the examples. The total settlement costs for each example were between $1,800.00 and more than $3,000.00.

[2] http://www.myfico.com/ The higher your FICO® credit score, the lower your payments!
Interest rates as of June 6, 2008:

30 Yr fixed mortgage

A change in the interest rate triggers a huge financial impact. Thus, the credit report is a product that if not properly matched to the consumer's specific credit needs, could cause serious harm to the consumer and potentially prohibit him/her from obtaining a loan. In today's mortgage environment, lenders need to be most concerned about obtaining the proper credit evaluation of their potential customers, looking deeper into the credit histories in an attempt to avoid some of the mistakes that are currently costing the industry billions of dollars.

Making sure this proposed rule does not prohibit the consumer or the lender from accessing the proper credit product for the specific needs of each consumer will be paramount to the long term success of HUD's stated objective in proposing these revisions to RESPA. Further, without protections of the credit report in this process, it will be impossible for HUD to continue its commitment to increase the opportunity of homeownership to many Americans.

Finally, HUD claims that its number one principle guiding this process is, "Borrowers should receive loan terms and settlement cost information early enough in the process to allow them to shop for the mortgage product and settlement services that best meet their needs" [3]. Ironically, the proposed rule itself as it applies to the credit report could easily wipe out all of the potential savings and interfere with the overall objective of HUD: expanding home ownership.

The remainder of this document addresses in greater detail each section of the proposed rule that NCRA finds problematic, and offer a suggest solution to what we deem the problem.

The proposed Good Faith Estimate (GFE)

The credit report is listed on the GFE as one of the many products and services needed to close a mortgage loan, all referred to as "settlement services". One of HUD's stated objectives in the title of this proposed rule is to "reduce costs" of these services; an objective that is both admirable and commendable. As NCRA has previously stated in this document, as it pertains to the credit report, saving money in this area comes at a very high risk.

The proposed rule allows for some settlement services, such as the credit report, to be listed on the GFE in a section that limits the variation of the fees in that section to a maximum variance of 10% between the GFE and the closing. By restricting the cost fluctuation of the credit report, HUD will be restricting many consumers' ability to obtain the proper report type required to

FICO®SCORE	ARP	Monthly payment
760-850	5.938%	$1.787
700-759	6.160%	$1,830
660-699	6.444%	$1,885
620-659	7.254%	$2,047
580-619	9.371%	$2,494
500-579	10.309%	$2,701
Example shows national average loan amount of $300K		

[3] Federal Register /Vol.73, No.51/Friday, March 14, 2008/Proposed Rules page 14031

accurately assess their credit risk. As HUD pointed out in the previously noted examples of settlement fees in the proposed rule, the fee for the credit report varied from $18.00 to $45.00.

Actual variations will be much greater, pending the consumer's credit history and need for verification of non-traditional data, something HUD has very recently encouraged lenders to do[4]. The cost of the non- traditional credit report as outlined by HUD in this notice, pending the amount of non-traditional data the consumer needs verified and scored, can easily cost between $75.00 to $150.00. Again, when comparing this cost to the consumer's potential savings in the interest on the loan, this cost can often easily be recovered in the matter of a of couple months. Sometimes the ability to obtain these reports can mean the difference in the loan actually being approved or denied.

Another factor that HUD must consider in restricting the credit report fees is the recent changes in the billing policies of the three national credit repositories with regard to the shopping of a consumer's mortgage loan by mortgage originators to lenders in an effort to obtain funding for the mortgage. New terms have been added to the credit reporting industry with the similar meaning to the above practice previously referred to as "joint use" of a credit report. They are now also known as "secondary use"[5]or "reissue", of the credit report.

This new term comes with a new price structure, one in which the mortgage originator, who will most likely have to pass on to the consumer a new credit report fee for *each* different lender who reviews the loan for potential funding. This means that the credit report fees previously discussed will be increasing by 100, 200, 300, maybe 1000 plus percent, pending the number of funding sources the mortgage originator needs to have review the consumer's credit history in search of funding[6]. This new fee structure makes it impossible to quote a fee for the credit report prior to knowing what the consumer's credit history is like and how many lenders they will need to shop the loan to for funding.

The solution to this problem is for HUD to create a separate line item for the credit report on the GFE, completely unrestricted from any limitations as to cost adjustments. While HUD may be concerned that this would open credit report fees to overcharges and abuse, that is unlikely as the credit report is unique; the consumer understands their specific needs in credit report documentation better than anyone else, as they alone know what is or is not accurate about their payment history.

As NCRA urged HUD in 2002[7], the credit report is unlike any of the other settlement services and the consumer should be allowed to be uninhibited in directing the lender in ordering additional credit products or services for their loan application, as they can easily understand these processes. The consumer almost always knows if they have paid the credit card bills on time or if a bill sent to a collection agency was paid. This may be an area in which any actions by

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[4] FHA Mortgagee Letter 2008-11 April 29, 2008 Non-traditional Credit Verification and Evaluation
[5] Ken Harney - Credit Report Fees on the Rise, *Washington Post* http://www.washingtonpost.com/wp-dyn/content/article/2006/12/15/AR2006121500858.html
[6] National Association of Mortgage Brokers position paper on secondary use of credit reports http://www.namb.org/Images/namb/GovernmentAffairs/Position_Papers/ReissueSecondaryUseFINAL.pdf
[7] See NCRA comments on the Proposed RESPA Rule, October 25, 2002

HUD that restricts the consumer's ability to obtain additional documentation for their loan may conflict with the goals of the Equal Credit Opportunity Act.[8]

Another unique aspect of the credit report that should allow HUD to manage it in a fashion different from other settlement services is that the credit report is recognized as being one of the most crucial of all consumer documents by the amount of legislation passed in attempts to assure the consumer's ability to obtain accuracy. There are multiple Federal laws that regulate the use of, the access to, and the ability for a consumer to dispute data on their credit report[9]. Despite all these attempts to regulate the credit reporting industry, debates continue about the level of credit report accuracy.[10] Increasingly, consumers are also turning to litigation as a means to settle inaccurately reported information on their credit histories as they loose faith in the ability to correct it with the national credit repositories.[11]

When it comes to the credit report, HUD would be doing the American consumer a great service and supporting HUD's primary mission by ascertaining that consumers have the ability to obtain, without any restrictions whatever, the type of credit reporting options necessary to properly document their payment history for the most complete evaluation of their own credit worthiness. Anything less than that is a grave injustice to the consumer and a breach of HUD's service to its mission.

The HUD 1 - Average Cost Pricing and Volume Discounts

Like the restriction on the credit reporting fees previously discussed, HUD's push for volume discounts on credit reports is risky. The aforesaid problems become compounded when evaluating the competitive balance of the credit reporting industry. Currently in the mortgage industry there is a standard that requires the data of all three national credit repositories to create a report when underwriting a mortgage loan.

The steep demand for the additional products and services in the creation of these reports, and the handling of consumers' disputes in a time frame that meets the demands of modern mortgage lending has created a sub industry of credit reporting companies that specialize in the production of the three repository mortgage credit reports. These firms must both purchase data from the national credit repositories on a wholesale basis and then compete with these same national repositories on a retail basis for the sale of mortgage credit reports to lenders. Due to the monopolistic power each of three repositories have by the required use of their data in each

[8] ECOA Subsection 202.6 (b) (6) Rules Concerning Evaluation of Applications

[9] Fair Credit Reporting Act, Fair and Accurate Credit Transactions Act, Equal Credit Opportunity Act, Fair Debt Collections Practices Act, Credit Repair Organizations Act, the Gramm-Leach-Bliley Act, etc.

[10] Testimony before the House Subcommittee On Oversight And Investigations Of The Committee On Financial Services by J.Robert Hunter, Director Of Insurance, Consumer Federation Of America May 21, 2008 on the The Impact Of Credit-Based Insurance Scoring On The Availability And Affordability Of Insurance. Also recently addressed in the Testimony Before the House Committee On Financial Services by Leonard A. Bennett, Consumer Litigation Associates, P.C. on behalf of National Association of Consumer Advocates, The National Consumer Law Center, and U.S. Public Interest Research Group May 20, 2008 regarding Examining the Need for H.R. 2885, the Credit Monitoring Clarification Act

[11] The National Law Journal, August 16, 2006 Tersa Baldas, Consumer Lawsuits Against the Credit Bureaus are Multiplying

mortgage credit report, since this standard was created in the early 1990's the mortgage credit reporting industry has had very obvious competitive issues.

In review of HUD's Regulatory Flexibility Analysis portion of the proposed rule, HUD notes that there is a "strong potential for a natural monopoly"[12] in the title industry, but fails to note the monopolistic problems of the credit reporting industry that currently exist and that have been well documented by both government[13] and Washington antitrust watchdog, American Antitrust Industry[14]. This monopolistic environment in credit reporting is not addressed any where by HUD in the 590 pages of the Regulatory Impact Analysis.[15]

The problems that this type of anti-competitive environment has created would be dramatically increased by the proposed rule's combination of the average cost pricing and the push for volume discounts. To be attractive to consumers, lenders would push for the cheapest possible average credit solutions which would be almost exclusively provided by one of the repositories, their mortgage reporting division, or the credit reporting subsidiary of a title company or lender. Historically, these entities have been able to provide much cheaper credit solutions due to owning the raw data or having an interest in other settlement services.

When one of HUD's objectives is to allow consumers to have the ability to shop for the services they want to use for settlement, it is counter-intuitive to create a rule that would help eliminate the high touch local service providers from being able to successfully compete for the consumers' credit needs. This lack of competition will undoubtedly lead to danger as some of these large volume providers are already sending their customer service departments to off-shore call centers.[16] As many people have experienced frustration with off-shore call centers for a variety of issues over the past couple years, just imagine the frustrations a consumer would have if the ability to obtain the American Dream of home ownership and the amount of interest they pay for loan hangs on the outcome of these types of call centers.

It is documented in HUD's Regulatory Flexibility Analysis that both HUD and the FTC studied consumer preference with regards to the way the GFE disclosed the Yield Spread Premium (YSP). NCRA urges HUD to perform some additional consumer research regarding the credit reporting options and a separate disclosure on the GFE for credit reporting line items. Consumers have been increasing purchases of many types of credit monitoring and credit disclosure products during recent years in an attempt to better understand their credit history and credit scores.[17] The

[12] Federal Register /Vol.73, No.51/Friday, March 14, 2008/Proposed Rules page 14107

[13] U.S. District Court for the Eastern District of Missouri, October 6, 1933 In Equity No. 10420, The United States of America vs. The National Retail Credit Association (This association was later known as the Associated Credit Bureaus, ACB, and is now known as the Consumer Data Industry Association, CDIA) et al. This Decree for violation of Antitrust law was renewed on several occasions until lifting in 1989.

[14] Competitive Problems in the Mortgage Credit Reporting Industry - September 9, 2002 American Antitrust Institute Jonathan Ruben http://www.antitrustinstitute.org/archives/files/264b.pdf

[15] HUD and the Office of Policy Development and Research – RESPA Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis FR-5180-P-01

[16] As reported in various Annual stockholder reports, SEC filings and business articles the repositories and the largest non-repository credit reporting agencies are all opening or experimenting with off shore based consumer call centers as a way to reduce operation costs.

[17] House Committee On Financial Services Hearing On Examining The Need For H.R. 2885, May 20, 2008 Testimony of: Robin Holland, Senior Vice President, Global Consumer Services, Equifax Inc

use of these "for fee" programs has been steadily growing at the same time the FACTA free annual credit reports have been available.

It is important to note that while these products and services help some consumers find issues related to their credit reports, the credit report scores provided in these direct to consumer programs are not the same as those used for the actual funding of a mortgage. Often they contain only the data of one of the three repositories, and only one program, myfico.com, offers the actual Fico brand credit scores used in mortgage lending. A study of the consumer preference in which type of credit reporting product or service offered in the mortgage process may very well confirm that, as in the open market, when they have a choice, the consumer would prefer to pay for a higher cost credit product or service to assure they are obtaining the best product or service for their needs.

Problems with HUD's Regulatory Flexibility Act Analysis (RFA)

There is very little documentation in the RFA regarding the impact to the credit reporting industry, other than estimates based on data regarding the credit reporting industry from the Census Bureau.[18] The 2004 data shows that there are 740 firms in the credit reporting industry, with a breakdown of the number of firms into different categories by the number of employees and annual revenues. The problem with these numbers is that they reflect the entire credit reporting industry with includes tenant reporting, employment reporting and other firms, and not just mortgage credit reporting agencies. Mortgage reporting agencies are highly specialized, utilizing the technology to produce the three merged repository mortgage credit report and interface that report with the mortgage lending systems used by Fannie Mae, Freddie Mac, and numerous other proprietary lenders' automated underwriting engines. When looking at this specific segment of the credit reporting industry, NCRA believes the best numbers on mortgage credit reporting companies can be found in Fannie Mae's DO/DU affiliate partner program which shows 151 companies as of June 8, 2008. [19]

This is a reduction since 2002 when there were approximately 300 companies in the mortgage credit reporting business.[20] By not addressing a decline of this magnitude in the number of credit reporting agencies that can actually provide a report for mortgage lending, and the complex market dynamic created by the monopoly powers in force, one must question HUD's estimates of the minimal impact this proposed rule will have on the credit reporting industry. While NCRA does not have the resources to provide exact numbers on the impact, we believe very strongly that

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[18] HUD and the Office of Policy Development and Research – RESPA Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis FR-5180-P-01page 5-111 V.D.2

[19] https://www.efanniemae.com/sf/refmaterials/creditproviders/index.jsp?sort=allByName
The actual number of companies represented on this site is 151, however, to come up the true number of mortgage credit reporting firms you must eliminate the 37 duplicate entries from the 151 listed. Many firms have multiple access points into DO/DU, have merged together and are in the process of merging technologies and have yet to eliminate one of the connections, (which can take several months) or may be the same company but marketing under more than one names. Our calculations after the reduction of these duplicates entries provides an estimate of 114 different companies in the mortgage credit reporting business on Fannie Mae's DO/DU site as of June 2008.

[20] See NCRA 2002 HUD RESPA Comments October 25, 2002

the $29-39 million dollar estimates representing a reduction of only 0.53%-0.72% of 2004 revenue[21] is ***significantly*** underestimated.

NCRA estimates (see Appendix A - Mortgage Credit Report Annual Revenue Estimates 2000-2008) the mortgage credit reporting industry revenues for 2008 will hit approximately $622 million, down from the record of $1.3 billion reached during the 2003 peak of the refinance boom. This represents about 3.45 million mortgage credit reports per month. NCRA membership[22] provides an estimated 70% of the credit reports used in mortgage lending. Considering the dysfunctional nature of the competitive balance of this industry as already addressed, an action by HUD like this proposed rule could easily have an impact of pushing 50% of the NCRA member volume to the largest 3 or 4 industry providers. This is reduction of hundreds of millions of dollars annually.

We urge HUD to not move forward on this proposed rule until this segment of the RFA can be recalculated using research specifically related to the mortgage credit reporting industry and taking into account the market powers that were missed in the first review.

Conclusion

NCRA urges HUD to heed its own words while moving forward with this rule: "Consumers have strong interest incentives to ensure they are getting the best deal possible on a mortgage loan and the associated third-party settlement costs, but poorly-informed decisions have drastic consequences"[23]. A poorly informed decision with regard to the credit report portion of this proposed rule could very well harm many more consumers than it helps. We are in agreement with HUD Director, Ivy Jackson's testimony to the Small Business Committee "Consumers need to know – *deserve* to know – what they are buying when they buy a home."[24] This is especially true when it pertains to the credit report used in the mortgage process.

NCRA does not support HUD's proposed rule as it is currently written. The credit report has far too critical an impact on the consumer to be included in any type program in which there are limitations placed upon the ability for the consumer to obtain the proper report needed because of price caps. The enticement for the cheapest possible solution to credit reporting services via volume discounts then highlighted by cost averaging may seem initially attractive; however, it is as full of pitfalls as the original RESPA problems HUD is endeavoring to fix. Consumers need to be protected from not being able to obtain the type of credit report that they deserve so that they may ascertain that the credit report matches their specific credit circumstances.

Quite simply, this can be accomplished by making credit an individual line item in the GFA (as it is on the HUD1-1A line 805) and not under the influence of price caps or volume price incentives that may create much greater losses than any savings the proposed rule could create. The plethora of Federal and state regulations regarding the credit report further the need for special

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[21] HUD and the Office of Policy Development and Research – RESPA Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis FR-5180-P-01page 5-113 V.D.3

[22] NCRA membership is currently 90 of the remaining 114 companies offering mortgage credit reports as identified in the Fannie Mae website in footnote 19.

[23] Federal Register /Vol.73, No.51/Friday, March 14, 2008/Proposed Rules page 14033

[24] House Small Business Committee Hearing Testimony of Ivy Jackson, May 22, 2008

treatment of this critical document. Let us not take chances with the vital credit report; the acquisition of a consumer's home hangs in the balance.

Further, while it is not HUD's responsibility to protect the credit reporting industry from anti-competitive practices, it is without question a lack in forethought to promote a proposed rule that increases those pressures. The continual reduction in the number of credit reporting companies will prove harmful to consumers in the long term. The competitive balance of the mortgage credit reporting industry is at stake with HUD's actions regarding this proposed rule. Please let your actions reflect your words and "ensure the honest settlement service providers can compete for business on a level playing field."[25]

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[25] Federal Register /Vol.73, No.51/Friday, March 14, 2008/Proposed Rules page 14031

Congress of the United States
Washington, DC 20515

September 16, 2008

The Honorable Jim Nussle
Director
Office of Management and Budget
Washington, D.C. 20503

Dear Director Nussle:

We are writing to urge you to reject the revised Real Estate Settlement Procedures Act (RESPA) proposal the Department of Housing and Urban Development (HUD) submitted to you for review as final in August 2008. Furthermore, we ask that you return the revised RESPA proposal to HUD with instructions to coordinate with the Board of Governors of the Federal Reserve (the Board), as well as other relevant federal agencies. We also think it prudent for you to instruct HUD to publish an advanced notice of proposed rulemaking for a final 60-day public comment period before submitting a final RESPA rule again to OMB.

RESPA and its implementing regulations govern settlement services for most residential purchase, refinance, and home equity mortgage transactions. The Act requires that consumers receive certain disclosures during the mortgage process, including the Good Faith Estimate (GFE) within three days of the loan application and the HUD-1 Settlement Statement at closing.

To our knowledge, HUD did not coordinate its efforts with the Board, which under the Truth in Lending Act (TILA) also has authority to revise mortgage disclosures. Therefore, it is likely that HUD's RESPA rule sent to you will conflict with other federal statutory and regulatory requirements under the Equal Credit Opportunity Act (ECOA) and TILA and could, if promulgated, confuse consumers who might receive multiple and conflicting disclosures.

As initially proposed by HUD, the modifications to RESPA would radically change the mortgage marketplace for consumers and industry. This prompted enormous public reaction – nearly 12,000 letters were submitted to HUD in opposition to its RESPA proposal, as published in the *Federal Register* on March 14, 2008. In addition, 242 Members of Congress, more than a majority of the U.S. House of Representatives, co-signed our August 7, 2008 letter to HUD Secretary Preston expressing our sincere concern with both the substance and the process for consideration of this very important issue. However, HUD's response to our letter lacked substance and assurances that HUD's revisions to its proposed RESPA rule would benefit homebuyers. We are attaching a copy of the letter for your consideration as you review HUD's revised RESPA proposal and determine what action to take.

Because no advanced notice of proposed rulemaking was issued, neither we nor the 242 Members who co-signed the RESPA letter to HUD nor the public have seen the version of the rule sent to OMB. Given HUD's record of attempted RESPA reform, we do not believe that any changes HUD made to its proposed RESPA rule, currently before OMB, will achieve our collective goal to streamline and simplify mortgage disclosures for homebuyers.

Given the significance of HUD's RESPA rule, it is critical that you delay its implementation and ensure that it is thoroughly vetted and tested before being finalized. As it stands, the rule has the potential to negatively impact homebuyers, the housing market, and our economy. This is a setback that none can afford -- especially during this time of market turmoil and uncertainty. Until there are assurances that HUD's revised RESPA rule will result in benefits that far outweigh any potentially negative consequences, a final RESPA rule should not be promulgated. Too much is at stake to rush quickly to judgment on an issue of such magnitude.

Again, we urge you to reject HUD's revised RESPA rule and send it back to HUD with instructions to coordinate with the Federal Reserve and other agencies.

Thank you for your consideration of our request.

Sincerely,

Rubén Hinojosa
Member of Congress

Judy Biggert
Member of Congress

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-0500

OFFICE OF GENERAL COUNSEL

September 12, 2008

The Honorable Melvin L. Watt
Chairman, Subcommittee on Oversight and Investigations
Committee on Financial Services
U.S. House of Representatives
Washington, DC 205150-6052

Dear Chairman Watt:

On behalf of Secretary Steven C. Preston, the Department of Housing and Urban Development (HUD) thanks you for the invitation to testify before your subcommittee on HUD's draft final rule that would amend HUD's Real Estate Settlement Procedures Act (RESPA) regulations for the purpose of simplifying and improving the process of obtaining mortgages and reducing settlement costs.

Unfortunately, the Department must respectfully decline this invitation. HUD's draft final rule was submitted to the Office of Management and Budget (OMB) on August 21, 2008, for review under Executive Order 12866 (Regulatory Planning and Review). Under the requirements of the executive order, signed by President Clinton on September 30, 1993, HUD may not discuss the content of the rule while under OMB review.

The executive order provides, in section 6(b), that only the Administrator of OMB's Office of Information and Regulatory Affairs (OIRA) can respond to oral communications initiated by persons outside of the Executive Branch of the Federal Government concerning the substance of a rule under OMB review. Accordingly, HUD would be unable, during the hearing, to discuss the content of the final rule, and, specifically, to advise of the changes that HUD made in response to public comments.

I can assure you, however, that HUD carefully reviewed the many thoughtful public comments received on the proposed RESPA rule, published on March 14, 2008, and HUD made changes to its proposed rule in response to public comments. Upon OMB's approval of the rule, HUD will make itself available to appear before your subcommittee to discuss the final rule.

Sincerely,

Robert M. Couch
General Counsel

cc: The Honorable Gary Miller

Committee on Financial Services
ATTN: Terrie Allison
Fax: (202) 225-4254

Hearing entitled, "HUD's Proposed RESPA Rule"
September 16, 2008

QUESTIONS FOR THE RECORD
Rebecca Borné
Center for Responsible Lending
November 11, 2008

1.

a. Should compensation for each actor in the mortgage settlement process (e.g. realtor, broker, settlement agent, lender) be disclosed?

We have particularly emphasized the importance of disclosure of broker compensation because of the unique role brokers play in the mortgage process and the demonstrated higher cost of brokered loans in the subprime market relative to loans from direct lenders. Moreover, and critically, disclosure will not sufficiently curb skewed incentives that make mortgage loans unnecessarily expensive—only substantive regulation will.

Brokers play a unique role in the mortgage market, justifying treating their compensation differently from that of direct lenders. First, borrowers tend to view brokers as special agents who are shopping among loans on their behalf. As a result, they are more likely to put trust in their broker and believe the broker is working to get them the best deal, rather than the one most profitable for the broker (that could in fact also be the worst deal for the borrower). In addition, the *incentives* driving the way brokers price loans are not the same as those driving lenders—brokers are selling a service, while lenders are selling a loan. Moreover, overwhelming evidence demonstrates that consumers in the subprime market pay significantly more for brokered loans than for direct lender loans,[1] driven largely by yield-spread premiums that do not result in corresponding reductions in upfront settlement costs in most circumstances.[2] For these reasons, we have emphasized that broker compensation should be disclosed in a simple, straightforward manner to, at the very least, alert the borrower to how much the broker is making on the loan. Such disclosure could lead some borrowers to understand that the broker is not necessarily working in the borrower's best interest. Regarding other actors in the settlement process, realtors already disclose their compensation relating to the property sale. Lenders, unlike brokers, are selling a product—the loan—and lender compensation is encompassed by the disclosure of the cost of the loan.

However, disclosure will not sufficiently curb the skewed incentives in the market. We discuss this reality in detail with respect to broker compensation in part b. below. It is true in other contexts as well. Permissible affiliated business relationships, for example, are required to be disclosed, but disclosure of the relationship in no way guarantees that consumers are not paying

considerably more for their loans because of the decreased competition often resulting from these relationships. In the case of fixed rate loans, which are commoditized and generally competitive, the profit gained by affiliated closing agents/attorneys, realtors, title companies, and other players, often exceeds what it would be without these relationships. HUD took a step in the right direction in its Proposed Rule by explicitly prohibiting tying an incentive *or a disincentive* to use of a referred settlement service provider.

b. Is the proposed RESPA rule for disclosure of yield spread premiums sufficient to serve this purpose and is it beneficial to consumers?

First and foremost, disclosure alone will not rein in abusive yield-spread premiums. Only substantive reform has the potential to do so. (In part c. of this answer, we discuss the broader skewed incentives created by yield-spread premiums and explain why we believe they should be prohibited as illegal kickbacks in certain contexts.) Second, even considering the limitations of disclosure, HUD's proposed disclosure is weak and should be much improved.

(i) *Disclosure alone is grossly insufficient.*

It is virtually impossible to disclose a way through the minefield of multiple loan terms simultaneously imposed with opposing impacts on the rate.

Among the most important—although unsurprising—findings of both the recent Federal Trade Commission study of homeowners' understanding of mortgage terms and Dr. Susan Woodward's recent FHA study was that consumers have more trouble understanding complex loan terms.[3] It appears as though, in working with the focus groups on the GFE, HUD resolved this quandary by designing a disclosure that assumes that all else would be equal in weighing the trade-offs. While that certainly makes for more streamlined disclosures, it does not change the fundamental problem. It only simplifies the disclosure—not the product, not the choices, and not the economic consequences of those choices. Moreover, since incentives drive markets, it is predictable that the options offered, and how they are offered, will be impacted by the brokers' own incentives. That is a structural problem, not a disclosure problem.

Were RESPA solely a disclosure law, it would be understandable for HUD to rely solely on trying to disclose a way through the murky, convoluted swamp of the impact of YSPs on loan pricing. Fortunately, RESPA is not solely a disclosure law, and HUD has the authority to address YSPs substantively. See part c. for further discussion.

(ii) *HUD's proposed disclosure should be much improved.*

Notwithstanding the limitations of disclosure, we appreciate HUD's effort to try to make the disclosure of broker fees more transparent. We agree that the current "required" disclosure of the yield-spread premium results in disclosure that is unclear and not uniform, if made at all. And we know that YSPs, and rate/point trade-offs in general, are so complex that disclosing them clearly is very difficult.

However, there are several significant problems with the proposed disclosure. First and foremost, it *presumes* a trade-off for the consumer through a reduction in upfront costs, which abundant research now proves does not occur except in limited circumstances.[4] A key goal of the broker disclosure should be to illuminate a common misconception rather than perpetuate it. We understand that HUD believes that the "Looking at trade-offs" table on page three provides protections for consumers. This table, though, assumes an environment of fixed and transparent pricing, which is not the reality of the subprime market. Consumers don't see originators' rate sheets. Originators may easily inflate the base rate and fill out the entire table, falsely indicating that the consumer is getting a fair-trade off—when in fact the same incentives are driving the same abusive practices.[5]

Second, the disclosure's characterization of the YSP as a "credit" only exacerbates the issue of the nonexistent trade-off. First, it suggests that this arrangement is somehow saving the consumer money, when it is in fact doing just the opposite. Second, the disclosure could actually end up advantaging brokers over lenders because many individuals will believe they are receiving something of value when they see a big number following the word "credit" rather than a zero.[6]

Third, the disclosure in no way makes clear that this is a fee paid to a broker. It never uses the word "broker" and tells the consumer nothing about the dynamic at play among the broker, the lender, and the consumer's loan costs. We believe there is some value derived from the sheer "sticker shock" that occurs when a consumer realizes how much the broker is making off the loan. This can trigger a discussion of loan options for the borrower.

Finally, the disclosure is confusing. We understand that HUD did several rounds of testing and believes it has adequately vetted the GFE. But HUD has not tested the effectiveness of this disclosure outside of controlled circumstances, and the discussion in the Proposed Rule does not suggest that HUD has tested the comprehensibility of this disclosure itself. Our attorneys with years of experience in the mortgage industry found this disclosure confusing. We find it very hard to believe that anyone other than the most sophisticated consumer will understand it.

We recommend that the following more simple and straightforward disclosure replace number 2 on the top of page two of the proposed GFE. This disclosure breaks out the portion of the broker fee paid directly by the consumer and the portion paid by the lender and recouped from the consumer through a higher interest rate:

Mortgage Broker Fees (see line 813 on GFE)* paid by you directly (included in settlement charges listed above):	$
+ additional fee received by broker from lender and paid by you through increased loan interest rate:**	$
Total Broker Fees:	$

c. What other concerns, if any, do you have about yield spread premiums or the disclosure of yield-spread premiums under RESPA?

During our testimony, we noted that the most important point we hoped to convey was this: *Yield-spread premiums can only be effectively and appropriately addressed substantively under RESPA's §8 than through disclosure.*

HUD holds to the position that the option to pay some closing costs through the rate should be available, but it also states that it "should be at the consumer's choice, based upon a complete understanding of the trade-off between up-front settlement costs and the interest rate."[7] The proposed GFE falls short of providing the information necessary for an informed choice, and even a perfectly designed GFE simply cannot ensure that such a trade-off exists.

HUD's policy position on YSPs rests on two underlying positions: (1) they can be a useful option to help pay some or all closing costs through the higher rate rather than financing them in the loan or paying cash upfront;[8] however, (2) payment solely for delivering a higher-cost loan to a lender is not a compensable service.[9] Unfortunately, empirical evidence now confirms that in the subprime, Alt-A, and FHA sectors, YSPs are often in exchange for exactly that—a higher cost loan, made so by a higher interest rate, no documentation, or a prepayment penalty.[10]

The irony with respect to prepayment penalties, of course, is that the public justification for them was that they were a price-trade-off that would result in a *lower* interest rate. Few consumers would knowingly choose to simultaneously pay a "rate-increasing" YSP and a "rate-reducing" prepayment penalty. Yet the subprime market was filled with loans with both prepayment penalties and YSPs.[11]

Dr. Woodward's recent study of FHA loans found that, except in the instance of true "no-cost" loans, YSPs are associated with higher, not lower costs. The net loss to those who pay YSPs ranges from $93 per $100 of YSP paid for brokered loans to $71 per $100 of YSP paid for mortgage bank loans.[12] Another study, released in 2007, showed that consumers only receive 25 cents in reduced fees for every one dollar paid in YSPs to brokers and that upfront fees are actually lower for retail loans than for brokered loans.[13] CRL released a study earlier this year that dramatically demonstrated the dichotomy between the prime and subprime markets.[14] The evidence from that study indicates that brokers in the prime market may help consumers find the cheapest deal, but that this is not the case in the subprime market. Brokered loans, when compared to direct lender loans, cost subprime borrowers additional interest payments ranging from $17,000 to $43,000 per $100,000 borrowed over the scheduled life of the loan. Even over a fairly typical four-year loan term, the subprime consumer pays over $5,000 more for brokered loans.[15]

A cornerstone of RESPA is the prohibition against fees for referrals or otherwise unearned fees under §8.[16] In enacting RESPA, Congress recognized that anti-competitive behavior, and unearned compensation, made the already expensive mortgage even more expensive. It adopted a combination approach—disclosure plus substantive regulations taking square aim at anti-competitive, market-distorting conduct. By simply providing strict conditions to ensure that YSPs are in fact an "alternative" way to pay costs, rather than simply a reward to brokers for

delivering loans with higher costs or riskier terms, HUD would give flesh to §8's intent to prohibit anti-competitive and costly market perversions.

In other contexts, we have recommended to regulators and legislators that YSPs be categorically prohibited in the subprime and non-traditional segments of the market, since experience and evidence demonstrate that YSPs do not result in a price trade-off in those segments. We similarly urge a specific rule stating that §8 bans YSPs in those segments.[17] But where allowed at all—whether just in the prime market, or in all markets if HUD does not ban YSPs in the subprime and non-traditional markets—it is necessary that HUD use the power RESPA already provides it to fix this broken system. Under existing RESPA §8 provisions, prescribing a set of specific conditions as to when YSPs are permitted is well within HUD's authority, carries out the letter and spirit of the law, will curb the abuses where they exist, will not adversely affect the portions of the market where they do not, and, finally, will ensure that the promised price trade-offs actually occur. We therefore recommend that the relevant portion of 24 CFR §3500.14 be amended to read:

> A yield-spread premium, or similar charge however denominated, may be permitted as *bona fide compensation* for services actually performed only where:
>
> (A) the mortgage broker receives no other compensation, however denominated, directly or indirectly, from the consumer, creditor, or other mortgage originator;
> (B) the loan does not include discount points, origination points, or rate reduction points, however denominated, or any payment reduction fee, however denominated;
> (C) the loan does not include a prepayment penalty; and
> (D) there are no other closing costs associated with the loan, except for fees to government officials or amounts to fund escrow accounts for taxes and insurance.

We note that one state, Massachusetts, recently enacted regulations which effectively prevented originators from using YSPs as a mechanism for self-rewards, although it was accomplished in a different way.[18] The reform does not appear to be restricting access to responsible credit in the state.[19] HUD should step to the forefront nationally and enact similar regulations.

We also note that the Federal Reserve Board, in its most recent amendments to Regulation Z, attempted to address YSPs through disclosure alone. It ended up withdrawing that part of its proposal after consumer testing demonstrated that its proposed disclosures were ineffective in addressing the injuries produced by YSPs. It has committed, as it continues its comprehensive review of Regulation Z, to "consider whether disclosures *or other approaches* could effectively remedy this potential unfairness [caused by YSPs]" (emphasis added).[20]

2. Should the GFE and the HUD-1 be the same format? If so, why? If not, why not?

The GFE should contain a summary page as well as more detailed supporting information that can be easily reconciled to the HUD-1. The summary page is important because the GFE and the HUD-1 serve two different purposes. The GFE is a shopping document that should provide easily digestible, clear, concise information about the loan to allow consumers to compare loans and alert them to the riskiest features of their loan. The HUD-1, on the other hand, should

provide a detailed account of all settlement costs. Despite their different purposes, easy reconciliation of the two forms is essential to the integrity of both the shopping process and the closing process. Consumers should be able to determine as easily as possible what has changed between the loan they were offered and the loan they sign at the closing table. With our comments on the Proposed Rule we submitted to HUD, we suggested a one-page summary GFE followed by a half-page summary of the HUD-1. This half-page summary would allow for feasible reconciliation between the GFE and the HUD-1. Our proposed form is attached to these responses as Exhibit A.

In the alternative, HUD could mandate, along with provision of the HUD-1 three days prior to settlement, an updated, final GFE summary page, as proposed by the National Consumer Law Center in its comments to HUD.

(In its Proposed Rule, HUD recognized the need for the GFE to be reconciled to the HUD-1 and added cross-references to the GFE on the HUD-1 to make it more reconcilable. We appreciate HUD's effort but think both options we suggest above would be easier for a consumer to follow than HUD's proposed cross-references.)

3. **What specific suggestions do you have as to how the RESPA rule issued by HUD and the TILA rule issued by the Federal Reserve should be harmonized?**

Coordination between HUD and the Federal Reserve to develop a single disclosure form is long overdue. While HUD disclosures focus on settlement costs and the Federal Reserve disclosures focus on the cost of credit, the two types of costs are inextricably intertwined. Disclosing them separately makes it easier for originators to manipulate the distribution of costs between these two "buckets" and make loans that are in fact excessively expensive appear affordable. Moreover, without integration, HUD's proposal steers consumers to shop based on settlement costs alone when, in reality, settlement costs make up a very small portion of the total loan cost.

Consumers should be able to evaluate all cost factors together in order to see the whole picture and make the most informed choice possible. These coming months, as the Federal Reserve continues its comprehensive review of Regulation Z, are an ideal time for the agencies to work together to develop an integrated approach, which should address the following issues:

a. <u>GFE</u>. The proposed GFE includes several disclosures that overlap with related, but not identical, TILA disclosures, which may be very confusing to consumers. HUD plans to use its Special Information Booklet to explain differences between the GFE and TILA,[21] but consumers are unlikely to read and process all four pages of the proposed GFE, much less an accompanying booklet. The two agencies should coordinate to develop one form. The following is a non-exhaustive list of components of any GFE on which the two agencies should coordinate to avoid confusing consumers.

   i. *<u>Initial loan amount/Amount financed</u>*. The proposed GFE includes the "initial loan balance," while the "amount financed" included in TILA

disclosures will be different if, as is common, the prepaid finance charges are financed as part of the loan.

ii. *Note rate/APR.* The proposed GFE requires the initial note rate while TILA requires the APR. The shopping document should include the APR because, while far from perfect, it is the only apples-to-apples figure that captures all finance charges, whether upfront or charged over time.

iii. *Monthly payment disclosure.* The monthly payment disclosure on the proposed GFE includes only principal, interest, and mortgage insurance, while TILA also allows creditors to include taxes and homeowners' insurance in the monthly payment disclosure.

iv. *Yield-spread premiums.* As noted earlier, the Federal Reserve recently looked at regulating YSPs through disclosure and recognized that its originally proposed disclosure-oriented broker rules were insufficient to curb abuses. While abusive yield-spread premiums should be substantively banned, any yield-spread premiums that remain permissible—for example, those associated with no-cost loans—should be disclosed in a simple, straightforward manner on an integrated GFE.

v. *Risky loan features.* HUD proposed listing some of the riskiest features of the loan on the summary page, including payment increases, negative amortization, balloon payments, escrow status, and prepayment penalties. Coordination with the Federal Reserve should not result in the removal of these important loan terms from the one-page integrated disclosure document. In addition, the page should increase emphasis on the total monthly payment, including an estimate of property taxes, property insurance, and other charges (currently included on page four of the proposed GFE); the first date on which the interest rate can rise; and clear notification that mortgage terms are negotiable.

b. Closing script. We commend HUD for its efforts to ensure consumers understand their loan terms by requiring a closing script. In our comments to HUD, however, we note several concerns we have about the closing script which must be addressed to ensure the script helps rather than harms consumers. Two of our concerns highlight the need for coordination between HUD and the Federal Reserve. First, the proposed closing script does not include the APR. Any closing script should include and explain the APR as the only price tag that includes both interest and fees. Second, the proposed script does not notify the consumer of his/her right to rescind. Any closing script should prominently disclose the consumer's three-day right to rescind for non-purchase money mortgage transactions, through language similar to that contained in the Right to Cancel Notice required by TILA.

c. **Average costing**. In its proposal, HUD appears to attempt to allow originators to charge the consumer an average cost while paying the third party settlement provider a different amount for each consumer. Some of these charges are used to calculate the finance charge under TILA and high-cost loans under HOEPA, and using average costs to compute them would undermine the accuracy of that calculation. We recommend that HUD clarify its proposal and ensure that average pricing—where the price charged to the borrower differs from that paid to the service provider—is not allowed; at the very least, though, it should coordinate with the Federal Reserve to ensure it is not further complicating or undermining the calculation of the finance charge.

4. **What additional actions should HUD take in the final rule related to RESPA to protect homeowners from abusive or predatory lending practices?**

   a. **Require an interest rate lock to allow consumers to meaningfully compare loan costs**. HUD absolutely must require an interest rate lock in order for the GFE to be effective. Without a rate lock, consumers must shop on settlement costs alone, which, again, are a relatively small component of total cost. Without an interest rate lock, it is too easy for originators to bait and switch consumers by presenting deceptively low settlement costs, only to recoup those costs by increasing the rate when the consumer returns a few days later. The large majority of prime rate lenders offer a *30-day* interest rate lock, which indicates that (1) the implementation cost of a required rate lock would be minimal; and (2) a 10-day rate lock is more than feasible.

   b. **Require that the GFE be binding for 30 days instead of 10**. Lenders should be able to predict settlement costs with a high degree of certainty for a 30-day period. In fact, settlement costs are unlikely to fluctuate at all within this time. Consumers must have early and binding disclosures in order to have a true opportunity to shop among loan options. As such, the GFE should be binding for at least 30 days instead of 10.

   c. **Refrain from encouraging the charging of fees for the GFE**. Expressly permitting originators to charge fees for the GFE may discourage comparison shopping, thus undermining competition. Further, RESPA prohibits charging a fee for completing the HUD-1,[22] and we are concerned that HUD's express allowance of a GFE fee will undermine RESPA by enabling originators to pass the cost of completing the HUD-1 on to consumers during the shopping phase. Lastly, HUD's position may misleadingly suggest preemption of state laws that prohibit nonrefundable application fees.

   d. **Impose tolerances on each item rather than on the aggregate cost**. HUD's proposed prescribed tolerances should help prevent unwelcome surprises at the settlement table. However, a 10% tolerance on each item, rather than in the aggregate, will better protect consumers.

e. **Strengthen protections related to the closing script**. While we support efforts to ensure that the consumer understands the mortgage, several protections are necessary to help ensure the script does not cause more problems than it solves. As noted earlier, the script should disclose and explain the APR and prominently disclose the consumer's three-day right to rescind for non-purchase money mortgage transactions. In addition, it should not have a consumer signature requirement, or, alternatively, the rules should clarify that the consumer's signature is not conclusive evidence that the disclosures were made. Further, HUD should clarify that the consumer has the right to rely on the accuracy of the closing script and that the lender is jointly liable for any inaccuracies in it.

f. **Ensure discounts are passed along to consumers.** We support volume-based discounts so long as those discounts are passed along to the consumer.

g. **Charge consumers an average price only when the originator pays an average price.** *Average cost pricing*, i.e., passing along a price paid to a third party as an average, is fine, but *average pricing*, i.e., paying a specific price to a third party but charging the consumer an average, is not and should not be allowed.

h. **Expand the revised required use definition to apply to all loan costs, not only settlement costs.** We have commended HUD for proposing to mandate true discounts on settlement costs when unaffiliated settlement service providers are required, but it is essential that the same principle apply to all loan costs.

i. **Update RESPA's servicing rules.** Given the array of servicing issues that have made an already disastrous mortgage market situation even worse, RESPA's servicing rules should be updated to include a duty to provide reasonable loss mitigation based on affordability; shorten the time period lenders have to respond to Qualified Written Requests from 60 to 14 calendar days; and provide transparency to consumers about their loan and servicing history.

j. **Amend the technical amendment regarding the servicing disclosure requirement to apply to all federally related mortgages, not only first liens, and revise the required disclosure to inform consumers of the broad role of servicers.** The statutory requirement applies to all federally related mortgages, not only first liens, and the regulation should do the same. Further, the required disclosure, which currently only mentions payment collection, must be significantly expanded to accurately convey the broad role servicers play.

5. **Are there other regulatory or legislative changes needed for RESPA?**

a. **Civil penalties, injunctive relief, and equitable relief for additional sections of RESPA.** RESPA violations are notoriously underenforced. We appreciate HUD's recognition that it needs additional statutory authority to enforce key disclosure provisions of RESPA, and we encourage Congress to provide civil

penalties for violations of sections 4 (HUD-1), 5 (GFE and special information booklet), 6 (servicing), 8 (prohibition against kickbacks, referral fees, and unearned fees), 9 (title insurance), and portions of 10 (escrow accounts), as well as the authority for HUD and state regulators to seek injunctive and equitable relief, as HUD plans to request.

b. **Private right of action.** Unless a private right of action, which would provide for actual damages and statutory remedies, is also included for all sections of RESPA, enforcement will continue to be minimal and RESPA violations will continue to be rampant throughout the industry. Given the volume of mortgage lending in this country, there will never be sufficient public resources to rely solely on public enforcement. Therefore, we urge Congress to add a private cause of action to RESPA, especially with respect to sections 4 (HUD-1) and 5 (GFE), by codifying that the violation of those provisions constitutes an unfair trade practice, as some states have done. Absent the availability of a private cause of action, relief to consumers taken advantage of by abusive lending practices is often completely out of reach.

c. **Expanded statute of limitations of three years**. We welcome HUD's plan to request an expanded statute of limitations and recommend that the time frame be three years. The troubles created by noncompliant loan disclosures often won't manifest themselves until the consumer has difficulty making loan payments, and three years is a reasonable time period to allow violations to come to light.

d. **Required delivery of HUD-1 three days prior to closing**. We have also commended HUD for seeking authority from Congress to require delivery of the HUD-1 three days prior to closing. Early receipt of the HUD-1 is vital to the consumer's ability to make a deliberate, informed decision about whether or not to close the loan.

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[1] *See, generally*, Keith S. Ernst, Debbie Gruenstein Bocian, and Wei Li, Center for Responsible Lending, *Steered Wrong: Brokers, Borrowers, and Subprime Loans* (April 2008), *available at* http://www.responsiblelending.org/pdfs/steered-wrong-executive-summary.

[2] *See, e.g.*, A Study of Closing Costs for FHA Mortgages, Prepared for U.S. Department of Housing and Urban Development, Office of Policy Development and Research, Prepared by Susan E. Woodward, Urban Institute at x (May 2008); Howell E. Jackson and Laurie Burlingame, *Kickbacks or Compensation: The Case of Yield-spread premiums*, 12 Stan. J.L. Bus. & Fin. 289, 309 (2007).

[3] James K. Lacko & Janis K. Pappalardo, *Improving Consumer Mortgage Disclosures*, p. 74-76 (Federal Trade Commission, Bureau of Economics Staff Report, June 2007). *See also* Ren S. Essene and William Apgar, "Understanding Mortgage Market Behavior: Creating Good Mortgage Options for All Americans," Joint Center for Housing Studies. Harvard University (2007).

[4] *See* Woodward FHA Closing Costs Study, *supra* note 2; Jackson and Burlingame, *supra* note 2.

[5] Indeed, that practice is sadly common in the auto sales world, where a buyer loses the value of a down payment or a trade-in "credit" by the seller's simple act of raising the price of the car and add-ons to "swallow the down" or "swallow the trade." As with mortgage transactions, the more pieces at play in the pricing game, the harder it is for the consumer to keep track of them all.

[6] There is an additional problem with labeling it a "credit" in RESPA, in that the RESPA documents are often used to calculate the finance charge and APR for TILA purposes, and RESPA labels can engender much confusion in translating fees from the GFE and HUD-1 into their proper place in the TILA calculations. The credit should be treated as an additional downpayment, reducing the principal, but should not affect the calculations of the finance charge or APR.

[7] 73 Fed. Reg. at 14041.

[8] *Id.*

[9] Statement of Policy 2001-1, 66 Fed. Reg. 53052, 53055 (Oct. 18, 2001) (Department affirms the 1999 Statement of Policy that "simply delivering a loan with a higher interest rate is not a compensable service.").

[10] The link is explained in greater detail in our comments to the Federal Reserve Board's recent proposed Regulation Z rules under HOEPA. Comments of the Center for Responsible Lending on Proposed Rules Regarding Unfair, Deceptive, Abusive Lending and Servicing Practices pursuant to the Home Ownership and Equity Protection Act (Docket No. R-1305) (April 8, 2008).

[11] Fully two-thirds (66.6%) of the subprime MBS market share for 2007 included prepayment penalties, down only slightly from 69.1% in 2006. Inside B&C Lending, p. 3 (Feb. 15, 2008). Even as overall subprime originations plummeted since August 2007, 47% of asset-backed securities issuances of 4Q07 included payment penalties. Inside B&C Lending, p. 3 (Feb. 15, 2008); Inside B&C Lending, p. 2 (Jan. 18, 2008).

[12] Woodward FHA Closing Costs Study, *supra* note 2, at x. In her report, Dr. Woodward cites one study which concludes that brokered loans were not more costly than retail loans. *Id.* at 15. However, the study does so based on a database of subprime loans made from 1995 to 2002, contributed by ten subprime lenders, *see* Amany El Anshasy, Gregory Elliehausen, and Yoshiaki Shimazaki, *Mortgage Brokers and the Subprime Mortgage Market,* at 7 (May 2004). The contributors are not identified, other than by membership in a particular trade association, and we are concerned that the data from a self-selected and limited group of originators may create some selection bias, making it an unsuitable database, or at least one which must be treated with great caution. We note that three major originators with dominant market shares over that six-year period (and who were members of that trade association during some or all of that period) were the subject of law enforcement actions, Household, Associates and Ameriquest. *These actions resulted collectively in over $1 billion in penalties and restitution.* Additionally, at least two other major lenders during the early years of that period utilized a similar business model to two of the law enforcement targets but collapsed in bankruptcy. If this study is to be considered in any regulatory decision, we urge that, at a minimum, HUD consult with regulators familiar with the business models and practices in which these lenders engaged during the period, to determine whether the illegal practices might have affected outcomes reflected in loans in that database, making the data unreliable for some purposes.

[13] Jackson and Burlingame, *supra* note 2, at 332; see also Patricia A. McCoy, *Rethinking Disclosure in a World of Risk-Based Pricing*, 44 Harvard J. on Legis. 123, 139 n.94 (2007) and sources cited therein.

[14] *Steered Wrong, supra* note 1.

[15] *Id.* That extra money, of course, is paid by the consumers in those subprime loans who could have—should have—been in the lower cost prime loans, and, but for the perverse incentives making those loans better for the middlemen, might have been.

Note that our data used in this study did not have any information on upfront fees paid by borrowers and, as a result, the cost of the loans is measured exclusively by interest rate. However, we also do not adjust for the cost of prepayment penalties, the overwhelming majority of which are on brokered loans. As a result, our estimates understate the true cost of brokered loans. *See* Appendix 4 of *Steered Wrong*. I n addition, we have seen no evidence to suggest that brokered loans carry lower upfront fees in such a way that would offset the higher interest payments we document. In fact, research suggests that the borrowers only receive 25 cents in reduced fees for every one dollar paid in YSPs to brokers and that upfront fees are actually less for retail loans than for brokered loans. *See Steered Wrong* at fn. 28. Finally, our estimates suggest that, on average, brokered loans for borrowers with credit scores of 640 or below pay an additional $3,146 per $100,000 amount in interest over a typical four year loan life. This is roughly the equivalent of an extra 3 percent of the loan amount in upfront fees. Therefore, even if these brokered loans did carry lower fees, it is extremely unlikely that they would be low enough to equalize the total cost of the loan.

[16] 12 U.S.C. 2607(a), (c)(2).

[17] Our comments to the FRB on its proposed HOEPA UDAP rules had offered specific definitions of subprime or higher-cost loans and "non-traditional loans" which HUD might adopt, or it might adopt the definition of "higher-cost loan" from the recently promulgated Fed HOEPA UDAP rules. CRL HOEPA Comment, *supra* note 11; Federal Reserve System, 12 CFR Part 226, Truth in Lending; Final Rule (July 30, 2008), 73 Fed. Reg. 44522, 44533.

[18] Commonwealth of Massachusetts Attorney General's Regulations, 940 MA ADC 8.06(17), Mortgage Brokers and Mortgage Lenders—Prohibited Practices.

[19] This regulation precludes brokers from accepting compensation where there is a conflict of interest—functionally a ban on YSPs as the regulations define that conflict. Shortly after implementation, Wells Fargo changed its broker compensation system from "a sliding fee based on loan's profitability to a flat 1.5% of the loan amount." Binyamin Appelbaum, *Most Lenders Accept Tough New Mortgage Rules in Mass*, Boston Globe, (Jan. 10, 2008). The Massachusetts rule appears to be working to eliminate the perverse market incentives that have grown up around this practice.

[20] 73 Fed. Reg. 44565.

[21] 73 Fed. 14037.

[22] 12 USC § 2610.

Hearing entitled, "HUD's Proposed RESPA Rule" September 16, 2008

QUESTIONS FOR THE RECORD

The House Financial Services Committee, Oversight and Investigations Subcommittee appreciates your participation in the hearing entitled, "HUD's Proposed RESPA Rule" held on September 16, 2008. Please provide written responses to the follow-up questions below within 30 days to be submitted as part of the hearing record.

Mr. GARY KERMOTT - American Land Title Association

1. Should compensation for each actor in the mortgage settlement process (e.g. realtor, broker, settlement agent, lender) be disclosed? Is the proposed RESPA rule for disclosure of yield spread premiums sufficient to serve this purpose and is it beneficial to consumers? What other concerns, if any, do you have about yield spread premiums or the disclosure of yield spread premiums under RESPA?

   Costs for settlement services are generally well disclosed on the HUD-1. Specific title related charges are individually disclosed in the 1100 series section of the HUD-1. This provides the consumer with a transparent and accurate accounting of what services are being provided and their costs. Under the proposed RESPA rule, yield spread premium disclosure is very confusing to consumers.

2. Should the GFE and the HUD-1 be the same format? If so, why? If not, why not?

   The GFE and the HUD-1 should definitely be in the same format. This allows the consumer to easily compare costs for specific settlement services. ALTA, NAR and CRL drafted a GFE that contained a cover summary cost page attached to a disclosure document that mirrors the HUD-1. This would give consumers the total costs of different settlement services in a summary format for shopping, while disclosing individual costs in the same format as the HUD-1. This is the most transparent method to ensure the consumer is given full disclosure of charges.

   For example, in some states title premiums are paid by the seller and in some states they are paid by the buyer. Without the areas on the GFE to disclose the individual costs, a consumer will be unable to make those comparisons. In addition, a summary only, or "package price" presentation on the GFE does not allow the consumer to understand exactly what services are included in the price. This is important in the purchase money transaction where a consumer's interests may exceed the requirements of a lender. Therefore, the most transparent disclosure format would be to mirror the GFE and the HUD-1 so that the benefit of existing full disclosure of costs on the HUD-1 can be shared with the consumer earlier in the transaction.

3. What specific suggestions do you have as to how the RESPA rule issued by HUD and the TILA rule issued by the Federal Reserve should be harmonized?

   Loan terms should be disclosed in a like manner. Under the proposed RESPA rule straight interest rates would be disclosed, while TILA forms would contain interest charges by the Annual Percentage Rate (APR). This would result in a consumer receiving two forms for the same loan that show different terms. This would be confusing to consumers. HUD and the FED should work together to produce one set of forms that contain both loan and settlement cost disclosures.

4. What is your estimate of the economic impact of the proposed RESPA rule on the land title industry and explain the basis of your estimate.

ALTA believes the estimate of HUD in its economic impact statement, while huge at over $2½ Billion, is still low. The impact of the proposed rule would be especially harmful to the great majority of our small business members, consisting of title agencies with two to sixteen employees.

5. Should the proposed RESPA rule allow real estate industry participants to offer incentives to create "one-stop shopping" for borrowers? Are certain industry segments hurt by the bundling of services? If bundling is not allowed, do you have other suggestions about how to reduce the costs associated with real estate settlements?

As discussed in Question 2, bundling may be harmful to some consumers, particularly in the purchase money transaction. There are many services that a consumer may need in these transactions that a lender who bundles services in its own interests may find unnecessary. They may include certain surveys, inspections or other consumer protective services. In a bundled transaction, the consumer would have no way of knowing whether they are receiving all the services they require. Any regulation should be moving in the direction of increased transparency, rather than less transparency.

6. Are there other regulatory or legislative changes needed for RESPA?

Currently, RESPA provides that the consumer can request the HUD-1 24 hours in advance of the closing, but provides no enforcement mechanism. Our closing and escrow officers are often provided with settlement and closing instructions minutes before scheduled closings. This is an inefficient and frustrating experience for our members and consumers. Congress should provide a real review period for consumers with a requirement that closing officers are provided with settlement documents from the lender a certain length of time before the consumer disclosure period. This would ensure that closers have adequate time to prepare accurate closing documents with time for consumers to review and understand them before signing. It would also provide consumers with an opportunity to contact their lender with questions about their loans before "the moving truck is parked outside" and pressure is high to sign any document, regardless of its terms.

Congress should also provide a private right of action for injunctive relief to competitors in the settlement services industry. Title agents often see violations of Section 8 of RESPA. Currently, their only recourse if to complain to HUD and their state regulators. If they were granted the right to an injunctive action against the violators, they could help self police the industry. This would relieve an already overburdened government enforcement ability and provide an enforcement mechanism much closer to where the violations are occurring. Such a provision would have to be carefully crafted to avoid spiteful or anticompetitive suits. Perhaps a 'loser pays" type of mechanism could be included in the language to ensure that only justifiable actions are brought to suit.

MORTGAGE BANKERS ASSOCIATION®
Investing in communities

Questions for the Record for Mr. David Kittle, Chairman, Mortgage Bankers Association
Hearing entitled "HUD's Proposed RESPA Rule"
September 16, 2008

1. **Should compensation for each actor in the mortgage settlement process (e.g. realtor, broker, settlement agent, lender be disclosed? Is the proposed RESPA Rule for disclosure of yield spread premiums sufficient to serve this purpose and is it beneficial to consumers? What other concerns, if any, do you have about yield spread premiums or the disclosure of yield spread premiums under RESPA?**

   Disclosure of Compensation – Direct charges to the borrower paid to each actor in the mortgage settlement process, as distinguished from compensation from other sources, should be disclosed, including the charges of the realtor, broker, settlement agent and lender. In addition, where a mortgage broker receives a yield spread premium (YSP), as compensation, based on the rate or terms of the loan from the lender, the broker should clearly disclose to the borrower the fact that the broker is being compensated by a lender and the amount of the YSP. MBA does not believe, however, that a lender should be required to make a similar disclosure of its compensation from the secondary market.

   This year, MBA published the attached paper "*Mortgage Bankers and Mortgage Brokers: Distinct Businesses Warranting Distinct Regulation,*" which was appended to my September 16 testimony, as Appendix D to MBA's comment letter.[1] The paper provides information on the differences between mortgage bankers and mortgage brokers.

   The paper points out that mortgage brokers are middlemen that facilitate or make arrangements for loans and that lenders, on the other hand, lend money. Consumers perceive brokers and lenders differently. Consumers regard mortgage brokers as shopping for them and ordinarily cease their own shopping when dealing with them, ceding the shopping to the broker. In contrast, consumers regard lenders (and their employees and agents) as providers of loan products which they shop and compare.

   Because mortgage brokers are regarded as shopping for borrowers, and may cause consumers to stop shopping, they present a great risk of steering consumers to a higher rate loan in return for a higher YSP. Accordingly, MBA believes it is appropriate for brokers to tell borrowers the compensation they receive from lenders. MBA does not believe that lenders or their exclusive agents warrant the same

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[1] The paper is also available on the Web at the following address: http://www.mortgagelenders.org/files/News/InternalResource/62646_Paper.pdf.

treatment because borrowers do not perceive them in the same way and they do not present the same risks.

Proposed (Now Final) HUD Disclosure – As indicated in our comment letter, attached to my testimony at the September 16, 2008 hearing, MBA does not believe the disclosure of YSPs in the proposed (now final) RESPA rule is sufficient to serve the purpose of a clear disclosure of broker compensation which would be beneficial to consumers. The rule requires that on the new GFE and HUD-1, lender and mortgage broker total charges be disclosed as "our origination charge" and the YSP disclosed as a "credit or charge for the interest rate of ___%."

MBA does not believe that the use of the term "originator" to cover lenders and brokers is helpful; the terms "lender" and "broker" on the other hand are understood by many borrowers. Moreover, treating the YSP as a credit does not make clear that the YSP is a payment from the lender based on the rate or terms of the loan.

While MBA appreciates HUD's efforts to clarify the function of a YSP in relation to the interest rate, MBA believes that this could be accomplished without creating confusing new terminology for broker fees. Also, some brokers may be paid on a basis other than a loan's interest rate and HUD's form does not encompass that.

MBA submitted a draft Combined Good Faith Estimate of Settlement Costs and Truth in Lending Act Disclosure (GFE-TILA form) and a draft Combined HUD-1 Statement of Settlement Costs and the Final Truth in Lending Act Disclosure (HUD-1-TILA form) with its comment to HUD and which it appended to my testimony of September 16.

MBA's draft GFE-TILA form discloses to the borrower in plain English the total compensation for the broker's services and the amounts paid by the lender to the broker on the borrower's behalf. It also makes clear that the amounts paid to the broker by the lender are paid by the borrower through the loan's interest rate and monthly payment.

MBA understands that HUD's approach to disclosure is shaped at least in part by concerns from mortgage brokerage industry advocates and the Federal Trade Commission (FTC) that the form should provide a "level playing field" between brokers and lenders. MBA believes that these assertions are incorrectly premised and obfuscate or do not fully comprehend the differing functions of and the differing consumer expectations regarding brokers and lenders respectively. This approach also does not appropriately address the consequently greater threat of steering by mortgage brokers. HUD's approach to disclosure has not been shared by other regulators.[2]

[2] Both the Board, prior to withdrawal of its proposal, and the FDIC have supported different approaches as shown in the HOEPA proposed rule and the comment letter on the HUD proposal from the FDIC.

2. **Should the GFE and the HUD-1 be the same format? If so, why? If not, why not?**

MBA believes the GFE and the HUD-1 should be readily comparable and in similar format so that consumers can easily compare the cost estimates provided on the GFE at the time of application to the final charges on the HUD-1 at settlement. The draft forms MBA submitted with its testimony accomplish this purpose and also incorporated the material in the current disclosure under TILA. These forms were developed by MBA members who make mortgage loans and day-in and day-out and who are presented with consumer questions.

In its final RESPA rule, HUD determined, however, to adopt dissimilar forms that include references on the final HUD-1 to the GFE's estimated charges. The rule also established a new third page to the HUD-1 which, in large part, provides a chart to compare GFE and HUD-1 charges.

MBA believes the use of these comparable forms throughout the mortgage process at shopping, at or following application, following underwriting and at and a day before closing is a better approach which would be more comprehensible to borrowers. It also believes that RESPA and TILA disclosures should be combined.

MBA is concerned that the three-page GFE in the final rule, though shorter than the four-page GFE originally proposed, is still too long. While it appreciates that the first page is intended to be a summary, and the second page a list of closing costs, MBA strongly believes that no matter how laudable the educational purposes of the form may be, the form's sheer length may cause borrowers to ignore its important information.

Borrowers are confronted today with a daunting pile of forms, from Government at all levels and originators. MBA believes HUD and the Board's efforts should be coordinated and focus on simplifying and combining disclosures.

3. **What specific suggestions do you have as to how the RESPA rule issued by HUD and the TILA rule issued by the Federal Reserve should be harmonized?**

Considering that disclosure of the costs and terms of mortgage credit are the responsibility of the Federal Reserve Board under the Truth in Lending Act (TILA) and the disclosure of settlement charges is the responsibility of HUD under RESPA, MBA believes that the best way of harmonizing the disclosures is to confine the HUD disclosures to settlement charges and the TILA forms to the terms and costs of credit. MBA believes the GFE and TILA disclosures then can be combined along the lines of the GFE-TILA form and the HUD-1-TILA form submitted with its comment and testimony. The forms embody how MBA would harmonize RESPA and TILA requirements.

The first page of the GFE-TILA form is similar to the second page of the HUD proposed GFE and lists the settlement costs. Importantly, it separately discloses lender charges and broker origination charges. The second page of the form

discloses the costs and terms of the credit in accordance with TILA requirements, including the Finance Charge and the APR (which are not included in the list of terms on the HUD forms). The HUD forms include the note interest rate and not the APR which will be confusing to borrowers when the TILA form is provided simultaneously under TILA.

The first page of the combined HUD-1-TILA form discloses the settlement charges attributable to the purchase transaction, the second page discloses the final settlement charges, and the third page discloses the final costs and terms of credit in accordance with TILA requirements.

HUD and the Board should work together to develop, reissue and simultaneously finalize joint rules and forms to simplify both the RESPA and TILA disclosures. MBA believes that only through combined, comprehensive reform can consumers take advantage of better transparency and at the same time lower costs. MBA also believes both HUD and the Board should involve industry and consumer advocates and other stakeholders to help the agencies shape their proposals and that they should utilize consumer testing to the maximum possible extent to ensure that improvements do in fact increase consumer understanding. Separate and potentially conflicting efforts will create more confusion for consumers and increase costs for everyone involved.

4. **What is your estimate of the economic impact of the proposed RESPA rule on the mortgage banker industry and explain the basis for your estimate?**

MBA has not arrived at its own cost estimates. Based on HUD's estimate, the costs of implementing the new GFE and HUD-1 will approach two billion dollars over the first two years considering retooling and recurring costs. Others have estimated costs higher than HUD's estimates.[3]

HUD's own Regulatory Flexibility Analysis estimates that the total one-time costs to the lending and settlement industries of the new GFE and HUD-1 alone will be $571 million, $407 million of which are estimated to be borne by small business.[4] HUD estimates that the total recurring costs are estimated to be $918 million annually or $73.40 per loan.

Even if HUD's cost estimates were accurate, the costs of TILA reform, anticipated shortly, are not included. TILA reform following after the estimated costs of RESPA reform are incurred, can be expected to result in duplicative costs of similar size for retooling, retraining, re-staffing and other costs to the industry. If the forms do not complement each other, recurring costs will increase considerably.

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[3] See, Ann E. Schnare, "The Estimated Costs of HUD's Proposed RESPA Regulations for the National Association of Realtors, (June 3, 2008).

[4] 73 Fed. Reg. 68262 (November 17, 2008).

If, on the other hand, RESPA and TILA changes are accomplished together, MBA believes significant economies would occur, resulting in lower costs as well as less confusion to borrowers.

In sum, considering the fragility of the market and the costs of industry changes including systems' conversions necessary to accommodate new requirements, as well as the need for borrowers to better understand both the terms of their loans and their costs, MBA strongly believes that HUD's forms should not be implemented until they are combined and harmonized with the Board's efforts to reform its TILA disclosures.

5. **Should the proposed RESPA rule allow real estate industry participants to offer incentives to create "one-stop shopping" for borrowers? Are certain industry segments hurt by the bundling of services? If bundling is not allowed do you have other suggestions about how to reduce the costs associated with real estate settlements?**

Allowing One-Stop Shopping - RESPA currently permits affiliated business arrangements as an exception to the general Section 8 prohibition against kickbacks, referral fees and unearned fees. This exception allows "one stop shopping" among affiliated settlement service providers as long as certain conditions are met. These include that a consumer referred to an affiliate receive a disclosure of the affiliation and that there be no "required use" of the affiliate. MBA does not believe it is necessary to change these provisions which permit affiliated arrangements to operate while also allowing competition from independent companies.

Harm From Bundling of Services – MBA has heard independent settlement service providers say they are harmed by the bundling of services. However, MBA is not aware of any recent study on this point. MBA favors maximum competition in the marketplace with affiliated and unaffiliated firms able to compete to provide innovation, choice and ultimately lower costs to consumers as long as arrangements are transparent and use of an affiliated settlement service provider is not required.

In its final RESPA rule, HUD changed the definition of "required use" so an economic disincentive that a consumer can only avoid by purchasing a settlement service from an affiliated provider would be as problematic under RESPA as an incentive contingent on a consumer's choice of a particular provider. The proposed rule indicates that it was particularly directed to use of homebuilder affiliates who tied a discount on a home to use of its affiliated settlement services provider, for example, a lender.

MBA believes that the formulation is too broad and may result in depriving borrowers of discounts that may indeed be *bona fide*. MBA believes it would be sufficient for HUD to indicate that under its current rules it may scrutinize discounts to assure they are *bona fide* rather than risking depriving borrowers of discounts altogether.

Other Suggestions in Lieu of Bundling – MBA does not believe bundling of services should be made illegal. As indicated, competitors offering bundled services should be able to compete in a transparent and free market.

In addition to permitting bundling, MBA believes disclosures, including those recently promulgated by HUD, should be improved considerably by combining TILA and RESPA required information. MBA believes that consumers need clear, useful information concerning mortgage offers so they can shop wisely and compare estimated costs to final costs.

MBA also believes that financial literacy efforts need to be vastly improved so that consumers can have a strong basis for understanding and utilizing information provided in disclosures.

6. Are there other regulatory or legislative changes needed for RESPA?

First and foremost, MBA believes legislative changes should be made, if necessary, to ensure that HUD and the Board of Governors of the Federal Reserve coordinate their reform efforts and that final disclosures are clear and truly useful for consumers.

As indicated, extraordinary and duplicative costs will come from separate, *seriatim*, reform efforts by HUD first and then the Federal Reserve. These costs will come at a time when the market is fragile and neither industry nor consumers should be forced to bear unnecessary and undue costs. If we are to proceed with mortgage reform, which MBA wholeheartedly supports, it is imperative that we do it right. Common sense dictates that HUD and the Board work together to reform all of the Federal disclosures to give borrowers the clearest, simplest information, under RESPA and TILA.

Additionally, MBA is developing several proposals to improve the regulatory process and restore faith in the mortgage market and the larger economy that will include proposals to vastly improve transparency and financial literacy, as well as regulation of the mortgage industry. As indicated in my testimony, our review of legislative improvements to the disclosure process, in particular, will be guided by the following principles:

- Disclosures should be streamlined and greatly simplified and uniform throughout the nation; terms that are not consumer friendly should be replaced with terms that are simple and understandable;
- Disclosures should be binding as early in the process as possible, considering that during the mortgage process information is developed and circumstances can change;
- The timing of disclosures should not result in undue delay for borrowers to receive needed credit;

- The process should facilitate competition to lower costs as well as the provision of high quality services;
- Borrowers and regulators should be appropriately empowered to prevent abuses; lenders should have a reasonable opportunity to cure errors prior to litigation; and
- Remedies for errors should not result in unduly increased costs for all consumers.

Hearing entitled, "HUD's Proposed RESPA Rule"
September 16, 2008

QUESTIONS FOR THE RECORD

The House Financial Services Committee, Oversight and Investigations Subcommittee appreciates your participation in the hearing entitled, "HUD's Proposed RESPA Rule" held on September 16, 2008. Please provide written responses to the follow-up questions below within 30 days to be submitted as part of the hearing record.

Mr. T. Anthony Lindsey – National Association of Realtors

1. Should compensation for each actor in the mortgage settlement process (e.g. realtor, broker, settlement agent, lender) be disclosed? Is the proposed RESPA rule for disclosure of yield spread premiums sufficient to serve this purpose and is it beneficial to consumers? What other concerns, if any, do you have about yield spread premiums or the disclosure of yield spread premiums under RESPA?

Homebuyers should be given a complete view of the charges they will incur when purchasing a home and obtaining a mortgage. An informed and educated homebuyer is best able to make the decisions that will result in an optimal outcome for themselves and their families.

2. Should the GFE and the HUD-1 be the same format? If so, why? If not, why not?

The GFE and the HUD-1 should be as synchronized as possible, mirroring each other to the fullest extent possible while maintaining their separate and intended functions. Consumers benefit when they can clearly compare the two documents and assess any differences in the charges put forth on the GFE and those they are paying on the HUD-1. Having the two documents mirror each other strongly aids in this purpose.

3. What specific suggestions do you have as to how the RESPA rule issued by HUD and the TILA rule issued by the Federal Reserve should be harmonized?

Our concern is less with the harmonization of the rules per se but rather the harmonization of the TILA statement and the GFE. We believe that consumer confusion can be limited if both documents are harmonized so that the TILA provides complete and understandable information about the loan while the GFE provides complete information about the settlement charges related to the loan. Industry groups have made great strides in creating model TILA/GFE combinations that work well together and explain charges and loan terms. It is should not be impossible to achieve in actuality.

In addition, the TILA statement should reconcile the confusion between the interest rate on the mortgage note and the "Annual Percentage Rate" (APR). The APR is often (if not always) higher than the stated interest rate because it encompasses other financing costs. At the very least, this should be clearly explained so that consumers do not confuse the APR with the note rate for the mortgage.

4. What is your estimate of the economic impact of the proposed RESPA rule on the realtor industry and explain the basis of your estimate.

We have not assessed the costs of the new rule. We did assess the costs of the original March 13, 2008 proposal. We believe the new rule's costs are less than the costs associated with the March 13, 2008 proposed rule because several costly elements have been removed, especially the closing script and related elements significantly reducing or eliminating costs to real estate agents. Nevertheless, retraining and technology modification costs remain for other industry participants. NAR has already begun developing education materials at some cost for its members.

What will be more costly is operating in the dark. We encourage HUD to provide clear guidance for implementation. Such guidance will abrogate the need for thousands of hours in legal fees to implement changes.

5. Should the proposed RESPA rule allow real estate industry participants to offer incentives to create "one-stop shopping" for borrowers? Are certain industry segments hurt by the bundling of services? If bundling is not allowed, do you have other suggestions about how to reduce the costs associated with real estate settlements?

Real estate industry participants should not be allowed exemption from the provisions of Section 8. They are already permitted to offer packages or a la

carte service offerings as long as savings are passed on to the consumer. Through this system price competition is maintained.

Competition amongst settlement service providers should be allowed to flourish. In many jurisdictions, the largest costs are not imposed by the settlement service providers but by the jurisdictions themselves. Transfer taxes, mortgage taxes, and other fees impact many transactions greatly. It is worth taking a second look at these costs and their impact on local housing markets and homebuyers and sellers.

6. Are there other regulatory or legislative changes needed for RESPA?

RESPA is a fairly well structured consumer protection statute. Its main shortcomings are that there is a lack of guidance and enforcement on key provisions. In some cases, we believe the statute is being enforced beyond its legislative intent, leading to confusion within the industry and conflicts in the courts. Aside from those instances, enforcement, though improved, remains generally light and aimed at large scale alleged violations. Greater guidance and enforcement on the more mundane RESPA violations would send a powerful signal to those in the industry who believe they can operate in the shadows and violate RESPA. We recommend HUD expand its provision of guidance closely tied to the plain meaning and Congress' intent in enacting RESPA. We also recommend increased enforcement of RESPA's core provisions to ensure that all settlement service providers operate on a level playing field.

Committee on Financial Services
September 16, 2008 Hearing

QUESTIONS FOR THE RECORD
Margot Saunders
National Consumer Law Center

1a. Should compensation for each actor in the mortgage settlement process (e.g. realtor, broker, settlement agent, lender) be disclosed?

Yes. It is important that consumers be provided the specific amount they are paying each actor in the settlement process. Consumers need this information in order to make informed choices. Regulators and lawyers representing consumers need this information in order to ensure Truth-in-Lending (TIL) compliance. Unfortunately, the final RESPA rule issued by HUD does not give either consumers or regulators the information they need. The final RESPA rule bundles all loan origination costs into a single line, and most costs of the settlement agent into another line.

As a result, the specific cost of the consumer's mortgage broker disappears, as both lender and broker-paid fees are included in the "origination" charge. Consumers are thus completely unable to determine exactly how much they are paying the broker. Bundling the cost of many services into the origination charge also creates significant hurdles for supervisory agencies and consumers when checking for compliance with the Truth-in-Lending Act. The same problem exists for settlement agent costs, although HUD has required some breakdown of the settlement costs on the HUD-1.

Disclosures are not enough to protect consumers by themselves. But they are an essential ingredient of a realistic and effective consumer regulation system. Substantive regulation is also necessary. Effective disclosures must mask real costs – their intended purpose is to provide needed information HUD's new rule unfortunately does not do that.

1b. Is the proposed RESPA rule for disclosure of yield spread premiums sufficient to serve this purpose [of disclosure] and is it beneficial to consumers?

No. The RESPA rule, as finalized, is actively misleading in its disclosure of broker premiums. HUD quite rightly recognized that existing disclosures of lender-paid broker compensation are inscrutable. However, HUD's insistence on characterizing lender-paid broker compensation as a credit to the borrower without any substantive regulation to make it so is nothing more than wishful thinking. Nor did HUD do any meaningful testing of the broker compensation disclosure; all of HUD's testing focused on having borrowers compare two loans that differed only by the total settlement costs, not along the three dimensions by which real-life loans typically vary: loan terms, interest rate, and total settlement costs. HUD relies for disclosure of the nuances of lender-paid broker compensation on an innovative and interesting tradeoff box Yet the tradeoff box also relies on the mischaracterization of lender-paid broker compensation as a credit to the borrower, does

not capture the full range of reasons for lender-paid broker compensation, and is optional for lenders to complete.

HUD's description of lender-paid broker compensation as a credit used to reduce settlement costs is inherently misleading. There is no requirement that the lender payment will actually be used in that manner. Nothing in the rule requires that brokers only be compensated through a yield spread premium or that the lender payment to the broker be offset against the total broker price charged to the borrower. Merely having the lender payment shown as a borrower credit to reduce the settlement costs will not make it function that way: Brokers can still charge borrowers a separate or increased fee.

It is simply not true, as HUD has emblazoned on the GFE and HUD-1, that a lender-paid broker payment reduces upfront costs. In most cases, according to studies HUD cites, lender-paid broker payments actually increase upfront costs.[1]

A more honest and transparent disclosure about the effect of the yield spread premium is illustrated below.

NCLC MODEL GFE DETAILS FOR BROKER COMPENSATION

MORTGAGE BROKER COMPENSATION	
Mortgage Broker Fees paid by borrower directly (included in settlement charges):	$ ________
+additional fee received by broker from lender and paid by borrower through increased loan interest rate:	$ ________
Total Broker Fees:	**$ ________**

Similarly, we have proposed that the tradeoff box, which can only be effective as a shopping tool if it is mandatory for all lenders to complete, be redone as follows.

You could ask us for other loans. This loan was based on our payment of some fees to your broker or other closing costs. The table below shows how this loan compares to loans where we pay your broker more or less money.

	This loan	If we don't pay the broker	If we pay the broker more money
Loan amount	$	$	$
APR	%	%	%

[1] Office of Pol'y & Dev , Dep't. of Hous. & Urban Dev., RESPA: Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis, FR-5180-P-01 Proposed Rule to Improve the Process of Obtaining Mortgages and Reduce Consumer Costs, 2-24 - 2-43 (2008).

Monthly payment	$	$	$
Maximum payment	$	$	$
How soon the interest rate can rise			
Maximum prepayment penalty	$	$	$
Maximum loan balance	$	$	$
Total settlement costs	$	$	$

The problem is not that brokers are paid out of the interest rate: the problem is that brokers are paid both out of the interest rate and out of pocket (or equity). HUD recognizes the costs borrowers incur when borrowers must shop both on fees and rate. Yet the rule substitutes disclosure for substantive regulation. If HUD were to require – as part of its regulation under RESPA's section 8 (12 U.S.C. Section 2607) – that lender-paid fees be actually credited to borrower's previously enumerated costs, then this mechanism might work as HUD envisions. But simply requiring a disclosure will not make the lender-paid fee provide a reduction dollar for dollar to the borrower.

1c. What other concerns, if any, do you have about yield spread premiums or the disclosure of yield spread premiums under RESPA?

Mortgage broker compensation is complex, confusing, and often needlessly expensive for borrowers. HUD's own studies indicate clearly that lender-paid broker compensation more often than not contributes to overpricing of all aspects of the loan. the broker fee, the settlement costs, and the interest rate.[2] That this overpricing is particularly prevalent for African Americans and Latinos[3] underscores the fundamental need for substantive limits on lender-paid broker compensation.

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[2] *E g.*, Susan Woodward, A Study of Closing Costs on FHA Mortgages, U.S. Department of Housing and Urban Development, Office of Policy Development and Research (2008), *available at* http //www.urban org/UploadedPDF/411682_fha_mortgages.pdf; *see generally* Office of Pol'y & Dev., Dep't. of Hous. & Urban Dev , RESPA: Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis, FR-5180-P-01: Proposed Rule to Improve the Process of Obtaining Mortgages and Reduce Consumer Costs, 2-24 - 2-43 (2008).

[3] *See* Robert B. Avery, Kenneth P. Brevoort & Glenn B. Canner, *The 2006 HMDA Data,* Fed Reserve Bull. A73, A96 (2007), *available at* http://www.federalreserve gov/pubs/bulletin/2007/pdf/hmda06final.pdf (pricing disparities between whites and minorities highest for broker originated loans); Robert B. Avery, Kenneth P. Brevoort, & Glenn B. Canner, *Higher Priced Home Lending and the 2005 HMDA Data,* Fed Reserve Bull. A123, A157-58 (2006), *available at* *http://www.federalreserve gov/pubs/bulletin/2006/hmda/bull06hmda.pdf* (same); Robert B. Avery & Glenn B. Canner, *New Information Reported under HMDA and Its Application in Fair Lending Enforcement*, Fed. Reserve Bulletin 344, 380, 394 (Summer 2005), *available at* http://www.federalreserve gov/pubs/bulletin/2005/3-05/hmda pdf (same), *cf.* Marsha J. Courchane, *The Pricing of Home Mortgage Loans to Minority Borrowers: How Much of the APR Differential Can We Explain?*, 29 J. Real Est. Res. 399, 400 (2007) ([M]uch of the explanation for why minority borrowers tend to have higher APRs than non-minority borrowers is because minority borrowers disproportionately take out subprime loans."); William Apgar, Amal Bendimerad & Ren S. Essene, Joint Ctr for Housing Studies, Harvard Univ , Mortgage Market Channels and Fair Lending: An Analysis of the HMDA Data 27, 37

In most circumstances, borrowers receive little, if any, benefit from lender-paid broker compensation. Only where the fees are either all in or all out of the rate are consumers able to shop successfully for the cheapest loan. When consumers can compare loans with the fees all *in* or all *out*, they are comparing loans with a limited number of variables. On the one hand is a loan with a particular rate and all fees required to be paid by the borrower – which would have to come from either cash or the home equity (meaning that the fees would be paid for in the loan, and more would be borrowed). On the other hand is the same loan with all of the fees paid through the interest rate – so no additional cash would required from the borrower and the loan amount would not have to be increased to cover the closing costs – yet the interest rate would be slightly higher. The latter loan is often called a "no-cost loan." This is somewhat of a misnomer because there are fees charged on these loans, and paid for by the consumer, only through a higher rate.

There are multiple benefits for "no-cost loans." These include the obvious – the retention of precious cash and equity by the borrower – as well as the lesser known finding that "no-cost" loans can result in a significant reduction of all closing costs as compared to other loans.[4] *However, the key to achieving this reduction is that the lender pays ALL of the fees.* The use of a combination of methods of payments – cash or home equity from the borrower plus lender paid broker compensation – has just the opposite effect: an increase in the closing costs and loan costs. Disclosure, by itself, does not overcome the cognitive dissonance caused by splitting the fees.

Most disclosures of lender-paid broker compensation are likely to confuse consumers, both because the tradeoffs are inherently complex and because borrowers are led to believe erroneously by both brokers and originators that brokers act as the borrowers' agents.[5] We concur with HUD that the yield spread premium should not be disclosed on a separate agreement. We share HUD's concerns that a separate agreement is likely to cause confusion to borrowers. We agree that the impact of any permissible yield spread premium must be clearly disclosed on the GFE However, HUD's use of the term "credit" to describe the lender-paid broker compensation, in the absence of substantive regulation that limits total fees, is misleading. Empirically, when there is a mix of both borrower-paid and lender-paid broker compensation, the total of all fees *increases*. When there is this

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(2007), *available at* http.//www jchs.harvard.edu/publications/finance/mm07-2_mortgage_market_channels pdf (white borrowers 50% more likely than African American borrowers to get a loan from a CRA-regulated entity within its CRA assessment area; failure to get a loan from a regulated institution within its catchment area increases the cost of the loan).

[4] Borrowers who use "no-cost" loans and so can shop on interest rate alone pay $1,200 less than borrowers who pay some lender or broker fees in cash. This suggests that consumers have a tougher time comparing alternatives when trade-offs are involved and that mortgage loan markets are not fully transparent or competitive. Susan Woodward, *A Study of Closing Costs on FHA Mortgages*, U.S. Department of Housing and Urban Development, Office of Policy Development and Research (2008.), available at http://www.urban.org/UploadedPDF/411682_fha_mortgages.pdf

[5] The Federal Reserve Board withdrew its proposed regulation of mortgage broker disclosure after consumer testing revealed that even when the disclosure included an explicit disavowal of the broker's agency, most consumers, even in a testing situation, without active misrepresentation by a broker, continued to believe that the broker, paid for by the consumer, was acting in the consumer's best interests. 73 Fed Reg. 44,522, 44,564 (July 30, 2008).

combination of methods of payments, there is not a one-for-one reduction in the borrower's costs, as the common understanding of the word "credit" would convey.

Lender paid broker compensation, when combined with borrower paid closing costs, is particularly troubling because it contributes to the widespread disparities in the pricing of home mortgage loans between whites and African Americans and Latinos. These disparities exist at every income and credit level and increase as income and credit levels increase.[6] In other words, the wealthiest and most credit worthy African Americans and Latinos are, compared to their white counterparts, the most likely to end up with a subprime loan. The origination channel – whether or not a loan is brokered – accounts for most of the difference in pricing.[7]

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[6] *See, e.g.*, Robert B. Avery, Kenneth P. Brevoort & Glenn B. Canner, *The 2006 HMDA Data*, Fed. Reserve Bull. A73, A97 (2007), *available at* http://www.federalreserve.gov/pubs/bulletin/2007/pdf/hmda06final.pdf (in 2006 and 2005, African Americans and Hispanics who received higher cost loans, on average, after accounting for borrower characteristics and lender, paid 20 and 10 basis points more, respectively, than white borrowers also in the subprime market); *see also* Marsha J. Courchane, *The Pricing of Home Mortgage Loans to Minority Borrowers. How Much of the APR Differential Can We Explain?*, 29 J Real Est. Res. 399, 417 (2007) (in 2005, African Americans and Hispanics who received subprime loans paid, on average, 50 and 17 basis points more, respectively, than whites in the subprime market); Debbie Gruenstein Bocian, Keith S. Ernst & Wei Li, Ctr For Responsible Lending, Unfair Lending: The Effect of Race and Ethnicity on the Price of Subprime Mortgages 11 (May 31, 2006), *available at* http://www.responsiblelending.org/pdfs/rr011-Unfair_Lending-0506.pdf *see also* Jim Campen, *Borrowing Trouble VII: Higher-Cost Mortgage Lending in Boston, Greater Boston and Massachusetts, 2005* at 8 (Mass. Community & Banking Council, Jan. 2007), *available at* www.masscommunityandbanking.org (highest income Latinos received high-cost home purchase loans at 6 times the rate of the highest income whites; highest income African Americans 7.6 times to receive a high-cost home purchase loan than highest income whites); Geoff Smith, Woodstock Institute, Key Trends in Chicago Area Mortgage Lending: Analysis of Data from the 2004 Chicago Area Community Lending Fact Book 10 (2006) (African-Americans and Hispanics more likely to receive high-cost loan than white borrowers, disparity increases as income increases); Elvin K Wyly, Mona Atia, Holly Foxcroft, Daniel J. Hamme, Kelly Phillips-Watts, *American Home: Predatory Mortgage Capital and Neighbourhood Spaces of Race and Class Exploitation in the United States*, 88 Geografiska Annaler, Series B: Human Geography 105 (2006) (finding geographic racial disparities in lending in Baltimore that cannot be explained by income); Stephanie Casey Pierce, Racial Disparities in Subprime Home Mortgage Lending: Can the Difference Be Explained by Economic Factors? (2006) (unpublished M. Pub Pol'y thesis, Georgetown University), *available at* http://www.dspace.wrlc.org/bitstream/1961/3612/1/etd_smc54.pdf (a survey of 2004 HMDA data from Louisiana found that blacks were 13.82% more likely than whites to receive a high cost, first lien purchase loan), *cf.* Robert B. Avery, Kenneth P Brevoort, & Glenn B. Canner, *Higher Priced Home Lending and the 2005 HMDA Data*, Fed. Reserve Bull. A123, A138 (2006) (piggyback loans more common in minority census tracts, even holding income constant), *available at* http://www.federalreserve.gov/pubs/bulletin/2006/hmda/bull06hmda.pdf.

[7] *See* Robert B. Avery, Kenneth P. Brevoort & Glenn B Canner, *The 2006 HMDA Data*, Fed. Reserve Bull. A73, A96 (2007), *available at* http://www.federalreserve.gov/pubs/bulletin/2007/pdf/hmda06final.pdf (pricing disparities between whites and minorities highest for broker originated loans); Robert B. Avery, Kenneth P Brevoort, & Glenn B. Canner, *Higher Priced Home Lending and the 2005 HMDA Data*, Fed. Reserve Bull. A123, A157-58 (2006), *available at* *http://www.federalreserve.gov/pubs/bulletin/2006/hmda/bull06hmda.pdf* (same); Robert B. Avery & Glenn B Canner, *New Information Reported under HMDA and Its Application in Fair Lending Enforcement*, Fed. Reserve Bulletin 344, 380, 394 (Summer 2005), *available at* http://www.federalreserve.gov/pubs/bulletin/2005/3-05/hmda.pdf (same); *cf* Marsha J. Courchane, *The Pricing of Home Mortgage Loans to Minority Borrowers: How Much of the APR Differential Can We Explain?*, 29 J. Real Est. Res. 399, 400 (2007) ([M]uch of the explanation for why minority borrowers tend

Lender-paid broker compensation creates the incentives that drive much of the racially disparate pricing.[8] By encouraging brokers to overprice loans where and when they can, lenders implicitly encourage brokers to target the vulnerable and gullible and those perceived as vulnerable and gullible. Most borrowers naively believe that their lenders will give them the loan they qualify for, and are insufficiently on their guard in dealing with brokers. African Americans and Latinos are particularly likely to believe that lenders are required to give them the best rate for which they qualify.[9]

The mechanics and extent of lender-paid broker compensation reach beyond simply overcharging African-American and Latino borrowers. Lenders use broker compensation to lock African-Americans and Latinos into downwardly mobile borrowing and destructive products For example, lender payments to brokers are often conditioned on the borrower's acceptance of a prepayment penalty[10] Thus, brokers have an incentive not only to put borrowers into a high cost loan in order to receive additional compensation from the lender, but to make sure the borrower is locked into the high cost loan. Prepayment penalties in these circumstances are seldom chosen by the borrower or in the borrowers' interest.[11]

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to have higher APRs than non-minority borrowers is because minority borrowers disproportionately take out subprime loans."); William Apgar, Amal Bendimerad & Ren S Essene, Joint Ctr. for Housing Studies, Harvard Univ, Mortgage Market Channels and Fair Lending: An Analysis of the HMDA Data 27, 37 (2007), *available at* http://www.jchs.harvard.edu/publications/finance/mm07-2_mortgage_market_channels.pdf (white borrowers 50% more likely than African American borrowers to get a loan from a CRA-regulated entity within its CRA assessment area; failure to get a loan from a regulated institution within its catchment area increases the cost of the loan).

[8] Debbie Gruenstein Bocian, Keith S. Ernst & Wei Li, Ctr. For Responsible Lending, Unfair Lending: The Effect of Race and Ethnicity on the Price of Subprime Mortgages 21-23 (May 31, 2006), *available at* http://www.responsiblelending.org/pdfs/rr011-Unfair_Lending-0506.pdf (discussing evidence and analysis that links pricing disparities with broker activity and incentives); *see also* Press Release, Office of the New York State Attorney General, Countrywide Agrees to New Measures to Combat Racial and Ethnic Disparities in Mortgage Loan Pricing (Dec. 5, 2006), *available at* http://www.oag.state.ny.us/press/2006/dec/dec05a_06.html (pricing disparities between whites and minorities highest for broker originated loans).

[9] Mortgage Foreclosure Filings in Pennsylvania: A Study by The Reinvestment Fund for the Pennsylvania Department of Banking 74 (Mar 2005), *available at* http://www.trfund.com/policy/pa_foreclosures.htm, *citing* Fannie Mae's 2002 National Housing Survey.

[10] *See* Debbie Gruenstein Bocian, Keith S. Ernst & Wei Li, Ctr. For Responsible Lending, Unfair Lending: The Effect of Race and Ethnicity on the Price of Subprime Mortgages 21 (May 31, 2006), *available at* http://www.responsiblelending.org/pdfs/rr011-Unfair_Lending-0506.pdf (noting that payment of yield spread premiums is often conditioned on the imposition of a prepayment penalty)

[11] Loans with prepayment penalties attached have higher rates of foreclosure, and in brokered loans, borrowers generally receive no interest rate reduction in exchange for the imposition of the prepayment penalty *See, e.g.*, Morgan J. Rose, Predatory Lending Practices and Subprime Foreclosures – Distinguishing Impacts by Loan Category 45 (Dec 2006), *available at* http://www.chicagofed.org/cedric/2007_res_con_papers/car_62_morgan_j_rose_foreclosures_draft.pdf (prepayment penalties and balloon notes combined on a fixed rate refinance subprime loan increase the rate of foreclosure 227%); Ellen Schloemer, Wei Li, Keith Ernst & Kathleen Keest, Ctr For Responsible Lending, Losing Ground: Foreclosures in the Subprime Market and Their Cost to Homeowners 21 (Dec. 2006), *available at* http://www.responsiblelending.org/pdfs/foreclosure-paper-report-2-17.pdf (higher risk for foreclosure for adjustable rate loans, loans with balloon payments, loans with prepayment penalties, and limited documentation); Gregory Elliehausen, Michael E. Staten & Jevgenijs Steinbuks, *The Effect of Prepayment Penalties on the Pricing of Subprime Mortgages* 15 (Sept. 2006), *available at* http://www.chicagofed.org/cedric/2007_res_con_papers/car_79_elliehausen_staten_steinbuks_preliminary

The key point here is – *Disclosure by itself is unlikely to remedy the systematic abuses of lender paid broker compensation that HUD identifies. Yield spread premiums should only be permitted when all costs are paid through an increased interest rate.* In all other circumstances, they should be banned.

2. Should the GFE and the HUD-1 be the same format? If so, why? If not, why not?

Somewhat. Because some of the detail required on the HUD-1 for review for TIL compliance is not useful for consumers for purposes of price shopping, the GFE need not be as detailed as the HUD-1 must be. However, HUD should have created parallel documents which – while not identical – would allow the reader to easily see how the early estimates in the GFE are comparable to the final charges disclosed on the HUD-1.

HUD should have, however, and failed to, require a summary sheet for the HUD-1 identical to the GFE. Referencing the GFE lines on the settlement statement is an important step, as is the provision of the "loan terms" box on the final page of the settlement statement. However, both of these require consumers to assemble information from several different sources in order to compare the information. This needlessly complicates consumers work.

3. What specific suggestions do you have as to how the RESPA rule issued by HUD and the TILA rule issued by the Federal Reserve should be harmonized?

There are two key problems with the relationship between the final rule and the Truth-in-Lending Act:

- Disclosure of the annual percentage rate, or APR; and
- Itemization of the amount financed, or, its inverse, the finance charge.

A. The Failure to Include the APR as the Key Loan Term on the GFE and Final Settlement Statement Undermines TILA and Limits the Effectiveness of the RESPA Disclosures.

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HUD is focused on reducing costs for consumers and facilitating shopping. The APR, in the mortgage market, is a necessity to achieve those goals.

The APR is the only apples-to-apples shopping metric in the mortgage market.[12] Its consistent use reduces the cost of consumer credit.[13] Consumers look for and rely on the

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pdf (finding that prepayment penalties were associated with higher interest rates unless they controlled for "borrower income, property value, loan amount, whether the loan was originated by a broker, and type of interest rate," in which case the difference shrank); *see also* Debbie Gruenstein Bocian, Keith S. Ernst & Wei Li, Ctr For Responsible Lending, Unfair Lending: The Effect of Race and Ethnicity on the Price of Subprime Mortgages 3-4 (May 31, 2006), *available at* http //www responsiblelending org/pdfs/rr011-Unfair_Lending-0506.pdf (the presence of a prepayment penalty increased the likelihood that African Americans had a higher cost subprime loan as compared to whites).

[12] *See, e.g*, Elizabeth Renuart & Diane E. Thompson, *The Truth, the Whole Truth, and Nothing But the Truth. Fulfilling the Promise of Truth in Lending*, 25 Yale J. on Reg. 181 (2008).

APR when shopping. In 2000, ninety-one percent of the population was "aware" of the APR.[14] More than seventy percent of the population reports using the APR to shop for closed-end credit [15] Seventy-eight percent of homeowners who refinanced their homes report comparison shopping on the basis of the APR.[16]

If the goal is to facilitate consumer shopping for mortgages, *HUD must mandate the inclusion of the APR on the GFE*. Interest rates are not as useful and can undermine the disclosure of the APR.

Interest rates, while reflecting the largest cost of credit, do not bundle all costs. Reliance on an interest rate in shopping can result in taking out the more expensive loan overall. Depending on the term of the loan, the fees, and how the rate is stated and calculated, interest rates can be inherently misleading and deceptive and quite often are not comparable with each other.[17] Moreover, interest rates do not control for the term of the loan.

Unlike interest rates, the APR takes the total cost of the loan, including fees and the time cost of money, and scales that cost to the size and term of the loan. The APR bundles the fees with the interest rate and standardizes the rate over an annual term. Thus, a shopper can tell whether a 15 year loan is cheaper than a 30 year loan by looking at just one number, no matter how many fees the lender has piled on at origination.

In recent years, the marketing of payment option ARMs has underscored the need for uniform disclosure of and reliance on the APR and the problems with the use of interest rates in disclosure. Payment option ARMs are typically advertised as, for example, "a 2% fixed rate" even though this rate may be fixed for no more than a day.[18] The APR, while it

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[13] *See* Victor Stango & Jonathan Zinman, *How a Cognitive Bias Shapes Competition: Evidence from Consumer Credit Markets* 3-4, Sept. 5, 2006, http://papers ssrn.com/sol3/papers.cfm?abstract_id=928956 (in markets where TILA disclosures made reliably, consumers who most underestimate APRs given a payment stream do not overpay on credit; in markets where TILA disclosures not made reliably, same consumers pay 200-400 basis points more for interest compared to consumers who underestimate APRs to a lesser degree)

[14] Thomas A. Durkin, *Credit Cards: Use and Consumer Attitudes, 1970-2000*, Fed. Res. Bull , 623, 631 (Sept. 2000), http://www.federalreserve gov/pubs/bulletin/2000/0900lead pdf.

[15] Jinkook Lee & Jeanne M Hogarth, *The Price of Money: Consumers' Understanding of APRs and Contract Interest Rates*, 18 J Pub. Pol'y & Marketing 66, 74 (1999)

[16] Jinkook Lee & Jean M Hogarth, *Consumer Information Search for Home Mortgages: Who, What, How Much, and What Else?*, 9 Fin. Services Rev. 277, 286 (2000).

[17] *See generally* Christopher L Peterson, *Usury Law, Payday Loans, and Statutory Slight of Hand: Salience Distortion of American Credit Pricing Limits*, 92 Minn. L. Rev. 1110 (2008)

[18] *See, e.g.*, Andrews v Chevy Chase, 240 F.R.D. 612 (E.D Wis 2007) (describing payment option ARM sold as having a fixed rate, when interest varied monthly; fixed rate is the payment rate); Complaint at 4, Fed'l Trade Comm'n v. Chase Financial Funding, Inc., No. SACV04-549 (C.D. Ca. 2004), *available at* http://www.ftc gov/os/caselist/0223287/040602comp0223287.pdf (adjustable rate mortgage with initial minimum payment, based on interest at 3 5% amortized over 30 years, which results in negative amortization, since actual interest rate is much higher, advertised as "3 5% fixed payment 30 year loan "); Gov't Accountability Office, GAO No. 06-1021, Alternative Mortgage Products: Impact on Defaults Remains Unclear, but Disclosure of Risks to Borrowers Could Be Improved 22 (2006), *available at* http://www.gao gov/new.items/d061021 pdf (describing advertisement for payment option ARM that

does not entirely reflect the risk of upwards adjustments in the interest rate, given problems with how it is calculated,[19] at least reduces the distortion, by requiring that the rate disclosed be a composite rate.[20] Composite rates reflect both an initial low rate and the rate that would be in effect but for the initial teaser rate.

Consumers cannot do the math to determine which of two loans is cheaper, given different rates, different fees, and different terms. The APR solves that problem and permits consumers to shop intelligently and efficiently. Failing to include the APR on the GFE obscures the cost of credit and hinders consumer shopping

It is no answer to suggest that consumers can rely on an early TIL disclosure for the APR. Even when the early TIL disclosure is provided, there is no penalty for providing an inaccurate TIL disclosure, whether accidentally or intentionally. As a result, many of the early TIL disclosures actually provided in the current marketplace are misleading.

Moreover, if the GFE is to have its maximum effect, it should be the single shopping tool for the mortgage. If consumers have to use multiple sheets to shop, the usefulness of the GFE is considerably diluted. Permitting multiple summary sources of critical information virtually guarantees that some consumers will ignore one or the other source. Ignoring the settlement costs and key loan terms reflected on the GFE would be undesirable. Ignoring the APR would be disastrous in most cases. Thus, if the GFE is to be used for shopping, disclosure of the actual APR must be mandated by HUD.

B. Either HUD Must Require Detailed Disclosure of All Costs or Congress and the Federal Reserve Board Must Revisit the Definition of the Finance Charge to Make It All-Inclusive.

The revision of the settlement statement, important as it is, potentially undermines the enforceability of the Truth in Lending Act (TILA). Enforcement of the TILA and the Home Ownership and Equity Protection Act (HOEPA) depend on full itemization of settlement costs. Remedies for the violation of TILA and HOEPA can include significant statutory damages and the right to rescind the loan, with the result of saving a home from foreclosure. In transactions to which RESPA applies, TILA rules say that the lender need not give an itemization of the amount financed if it provides both the GFE and settlement statement.[21] The itemization of the amount financed is essential for regulators, consumers, and their advocates to determine if TILA's fundamental disclosures–the APR, the finance charge, and the amount financed–were made correctly. Mortgage lenders consistently use the GFE and settlement statement as a replacement for the itemization of the amount financed

promised 45% reduction in monthly mortgage payments and interest rate of 1 25%; interest rate of 1.25% only applied for first month, and this fact disclosed in "much smaller print" on second page).

[19] Patricia A. McCoy, *Rethinking Disclosure in a World of Risk-Based Pricing*, 44 Harv. J on Legis. 123, 143-44 (2007) (discussing limitations of variable rate disclosures in detail).

[20] 12 C F.R. §226.17, Official Staff Commentary, §226.17(c)(1)-(10).

[21] Official Staff Commentary on Regulation Z, § 226.18(c)-4

HUD has required lenders to disclose as a lump sum all origination charges and most title services.[22] This is certainly an improvement from the perspective of price comparison. However, not all origination services and title services are clearly all-in or all-out of the TILA finance charge. The Federal Reserve Board has allowed the finance charge to become debundled[23] Under the statute, for example, title insurance is excluded from the finance charge.[24] Other charges related to title insurance, including the settlement fee, courier fees, or document preparation fees, may be included in the finance charge, however, particularly if they are not bona fide and reasonable.[25] Similar inconsistencies plague other origination fees.[26]

The treatment of the lender payment to the broker as a credit also potentially complicates TIL review. Without guidance from the Federal Reserve Board, it is not entirely clear what effect treating the lender paid broker compensation as a borrower credit will have on the central TIL disclosures, the finance charge and the APR. The credit should be treated as an additional down-payment that reduces the principal loan amount but is otherwise neutral as to the calculation of these central disclosures. Yet without guidance from the Federal Reserve Board, the use of the word "credit" opens up a litigation minefield and likely increases costs for all parties.

HUD's rule on average charge pricing also undercuts TIL review. There is no clear authorization in the TILA for charging a finance charge based on an "average charge," when the actual price is known and ascertainable. Permitting these fees to be disclosed as average charges opens up a litigation minefield. Neither consumers and their advocates nor lenders will be able to tell from a HUD-1 what the actual finance charge amount of many fees is.

Absent coordination with the Federal Reserve and statutory changes there is no guarantee that all bundled fees are either all in or all out of the finance charge. Thus, the newly revised settlement statement potentially obscures determination of the TILA finance charge and amount financed.

4. What additional actions should HUD take in the final rule related to RESPA to protect homeowners from abusive or predatory lending practices?

HUD should have, and failed to, take the following steps in the RESPA rule to protect consumers from abusive practices.

- Mandate an interest rate lock;

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[22] 73 Fed. Reg 68204, 68244-45 (Nov. 17, 2008) (final rule), 73 Fed. Reg. 14030, 14060 (Mar. 14, 2008) (proposed rule).

[23] *See, e g.*, Elizabeth Renuart & Diane E. Thompson, *The Truth, the Whole Truth, and Nothing But the Truth: Fulfilling the Promise of Truth in Lending*, 25 Yale J on Reg. 181 (2008).

[24] 15 U.S C. § 1605(e)(1)

[25] *See generally* National Consumer Law Center, Truth in Lending §§ 3.9.5, 3 9.6 (6th ed. 2007.)

[26] Most origination fees, aside from the ones HUD requires separately disclosed in the 800 series, are probably finance charges. However, some commonly charged fees, such as appraisal review fees, could be excluded from the finance charge in some circumstances and are not clearly required by HUD to be disclosed separately from other origination charges. Official Staff Commentary on Regulation Z, § 226.4(c)(7)-1

- Extend the binding period for the GFE from 10 business days to 30 days;
- Prevent lenders from gaming the system by holding them to the disclosures, instead of permitting cure at-will for 30 days after closing;
- Clarified that its allowance of credit report fees before the provision of a GFE was not meant to preempt state law;
- Impose tolerances on the individual items rather than an aggregate;
- Required average cost pricing rather than average charge pricing; and
- Expand the required use definition to apply to all service providers, not merely affiliates.

5. Are there other regulatory or legislative changes needed for RESPA?

Yes. RESPA, although enacted with the noblest of intentions, lacks built in incentives to ensure compliance. **There is much that Congress can do to improve the settlement process in this nation by passing statutory changes to RESPA that would beef up enforcement.**

A. Civil Liability under RESPA and a Uniform Statute of Limitations Would Greatly Enhance Compliance

Without a private right of action to enforce the timing and content of both the GFE and the HUD-1 under sections 4 and 5 of RESPA, a borrower's leverage to negotiate loan terms and ensure fairness in the marketplace is severely limited Civil enforcement of each element under the new rule, especially the GFE and HUD-1 requirements, is essential in order to raise levels of compliance and thus ensure a better functioning market. We also support HUD in seeking a statutory requirement that the final HUD be delivered before closing.

We support HUD's intention to seek statutory modifications including authority for imposition of civil penalties for sections 4, 5, 6, 8, 9, and 10 of RESPA, as well as authority for the Secretary and state regulators to obtain injunctive and equitable relief under RESPA. Better enforcement mechanisms should result in some better compliance with these requirements and the ability of state regulators to supplement the work of HUD is important.

Increased government enforcement, however, still leaves borrowers who were victims of "bait and switch" or other abusive lending with no recourse under RESPA sections 4 and 5 to directly challenge some of the main loan disclosures used to deceive them about loan terms. This is especially a concern in light of the new GFE cover page. Without proper consequences for significant changes between the GFE cover page and the final loan disclosures, the GFE could be used as a tool to promote bait and switch regarding loan terms, as well as settlement costs, rather than for shopping. It could affirmatively aid in borrower deception because any misrepresentations would not be able to be stopped or challenged by the borrower. While undoubtedly some lenders would be deterred or punished through regulatory enforcement, the reach of regulatory measures is inevitably limited. As HUD itself points out in the proposed rule, without enforcement authority and clear remedies, consumers are less protected and the statute is much less effective. The

remedy most likely to result in compliance is a private action by the borrower. Civil enforcement is a compliance incentive.

B. Section 8(b) Should Prohibit Overcharges, Not Only Markups.

Section 8(b)'s prohibition should apply to overcharges as well as markups. HUD has rightly indicated in its 2001 Statement of Policy[27] that unreasonable fees, even where a markup of a third-party fee is not involved, are prohibited under Section 8. We applaud HUD's inclusion of this approach in the Policy Statement, but unfortunately compliance with this provision has been limited. Every year, there are significant numbers of reported cases under Truth in Lending discussing unreasonable closing costs. We recommend that Congress clarify this by statutory language. TILA requires the overcharges to be correctly disclosed as part of the finance charge and the APR; yet, as a disclosure statute TILA does not limit the amount of the overcharge.[28] RESPA could and should provide this essential consumer protection.

C. Escrow Collection Should Be Limited to the Amount Owed and Payments on Taxes and Insurance Should Continue Even Where the Borrower Is 30 Days Late

Currently, servicers administering escrow accounts are permitted to collect payments so that the total paid on one year includes two extra months' of funds. This practice has a particularly negative effect on homeowners who live on tight budgets, and the practice is not grounded in any reasonable expectation that such a cushion is necessary Problems in escrow payments too often result in borrowers falling behind in their mortgage payments because the additional cost of taxes and insurance may not have been properly included in the underwriting, or because the cost of escrow has increased over time. For these homeowners, the requirement of paying more than what is required to cover the month's payments is onerous and unwarranted. *We recommend that Congress change the rule so that only amounts owed can be collected through escrow.*

Moreover, *we recommend that either HUD or Congress clarify that a servicer must make escrow payments even where a homeowner is 30 days late on a payment.* We believe that the statute clearly requires that escrow payments must *always* be made by the servicer. The regulatory exception to this rule is completely unwarranted and causes substantial hurdles for borrowers seeking to straighten out their payments. Specifically, one payment made 30 days late is enough to jeopardize the borrower's homeownership if taxes go unpaid, fees and costs are then added to the tax bill, potentially doubling the tax bill At that point, a small default – a late payment – may become insurmountable. This is especially a concern where one unpaid late fee could result in a borrower being categorized as 30 days late, even where all the relevant monthly payments for that month were paid on time and in full and where the late fee itself was incurred for paying late but substantially before the 30 day mark. This occurs because a borrower who owes a late fee but only sends in the usual monthly payment generally will have the payment applied first to the late fee and then to principal and interest, thus leaving insufficient funds to cover the regular payment. As a result, the monthly

[27] Real Estate Settlement Procedures Act Statement of Policy, 2001-1, 66 FR 53052 (Oct 18, 2001)
[28] 12 C.F.R. 226.4(c)(7).

payment is not paid in full and is considered late. Borrowers who are 30 days late generally are not on their way to default. Interrupting escrow makes returning to on-time status harder to achieve -- an unnecessary result

D. RESPA's Servicing Rules Must Be Updated

Recent litigation challenging abusive mortgage servicing[29] and the challenges faced by borrowers in the current foreclosure crisis make it clear that RESPA's servicing provisions need to be enhanced and updated While HUD's current proposed rule focuses primarily on loan origination issues, some of the legislative changes HUD seeks look toward the post-origination phase. Escrow and servicing issues are essential to maintenance of a functioning mortgage market and to foreclosure prevention. In the current crisis, it is the servicing issues that have become paramount, yet the right to get a fair deal from a servicer is not uniformly enforceable and too often is out of reach for homeowners.[30]

- *First, RESPA must include a duty to provide reasonable loss mitigation prior to any foreclosure that prioritizes "home-saving" loss mitigation options over those that result in loss of the home* Any loss mitigation must be based on an affordability analysis that considers the borrowers debt to income ratio and residual income—to ensure enough actual dollars for non-housing expenses—as well inclusion of the borrower's full debt profile, including junior liens on the property.

- Additionally, loan modification or forbearance agreements often contain a waiver of claims provision that purports to release the servicer and holder from any past or future claims that the borrower may have. Broad release language potentially cuts off

[29] *Islam v Option One Mortg. Corp.*, 432 F. Supp. 2d 181 (D. Mass. 2006)(servicer continued to report borrower delinquent even after receiving the full payoff amount for the loan); *Hukic v. Aurora Loan Servicing, et al*, 2006 WL 1457787 (N.D. Ill. May 22, 2006)(servicer=s clerical error in recording amount of payment left homeowner battling with subsequent servicers and fending off foreclosure for nearly five years); *Rawlings v. Dovenmuehle Mortgage, Inc , 64 F. Supp. 2d 1156* (M.D. Ala. 1999)(servicer failed for over 7 months to correct account error despite borrowers' twice sending copies of canceled checks evidencing payments); *Choi v. Chase Manhattan Mortg. Co.*, 63 F. Supp. 2d 874 (N D Ill. 1999)(home lost to tax foreclosure after servicer failed to make tax payment from borrowers escrow account and then failed to take corrective action to redeem the property); *Monahan v. GMAC Mortg. Co.*, 893 A.2d 298 (Vt. 2005)(affirming $43,380 jury award based on servicer's failure to renew flood insurance policy and subsequent uninsured property damage); *Norwest Mortgage, Inc. v. Superior Court*, 85 Cal. Rptr. 2d 18 (Cal. Ct. App. 1999)(kickbacks available in force-placed insurance encourage placement); *Vician v. Wells Fargo Home Mortg.*, 2006 WL 694740 (N D Ind. Mar 16, 2006) (servicers have forced-placed insurance in cases where the borrowers already had it and provided evidence of it); *Dowling V. Select Portfolio Servicing, Inc.*, 2006 WL 571895 (S.D. Ohio Mar 7, 2006) (servicers have forced-placed insurance in cases where the borrowers already had it and provided evidence of it); *accord, Barbera v WMC Mortgage Corp* , 2006 WL 167632 (N D. Cal Jan. 19, 2006).

[30] These recommendations are incorporated in detail in H.R 5679, The Foreclosure Prevention and Sound Mortgage Servicing Act of 2008, introduced by Representative Waters. NCLC has directly endorsed this legislation, it is a clear roadmap of some needed changes to RESPA's servicing rules. *See also* Written Testimony of Tara Twomey, National Consumer Law Center, also on behalf of National Association of Consumer Advocates, Before the United States House of Representatives Subcommittee on Housing and Community Opportunity, H R 5679, The Foreclosure Prevention and Sound Mortgage Servicing Act of 2008 (Apr 16, 2008), *available at* http://www.nclc.org/issues/predatory_mortgage/content/TwomeyHR5679Testimony.pdf

all claims the borrower may have related to the origination or servicing of the loan; it must be banned. *RESPA also should prohibit the equally abusive practice of forcing borrowers to arbitrate any disputes with the lender or servicer.*

- Further, the current rules for responding to Qualified Written Requests do not allow a borrower to receive timely, useful information, nor do they prevent against foreclosures occurring before a response arrives. While RESPA currently requires servicers to respond to borrowers' request for information and disputes within 60 days, in practice many such inquires go unanswered. *RESPA should require that servicers respond to borrowers inquiries and disputes within 14 calendar days.* With a shorter timeline, a corresponding statutory change could then be made to remove the requirement for servicers to acknowledge receipt of QWRs. This timeline also would make it less likely that foreclosures would occur while QWRs are outstanding. *RESPA also should be amended to provide transparency to the servicing process by allowing the homeowner to obtain key information about the loan and its servicing history* Such information should include:

    - whether the account is current, or if not, the date the account went into default;

    - the current balance due on the loan, including the principal due, an itemization of all fees due, an explanation of the escrow balance, and whether there is any escrow deficiency or shortage;

    - a full payment history showing in a clear and easily understandable manner all the activity on the home loan since the origination of the loan, including the escrow account, and the application of payments;

    - the initial terms of the loan; a copy of the original note and security instrument;

    - identification of the owner of the mortgage note and any investors;

    - any documents that limit, explain or modify the loss mitigation activities offered by the servicer; and

    - any other information requested by the homeowner reasonably related to loss mitigation activities.

Finally, homeowners often have difficulty determining which address of the servicer is the correct one for sending QWRs. *RESPA should provide that any QWR received by the mortgagee or servicer is considered valid,* even where sent to an address other than one designated by the mortgagee or servicer for receipt and handling of such requests.

Hearing entitled, "HUD's Proposed RESPA Rule"

September 16, 2008

QUESTIONS FOR THE RECORD

The House Financial Services Committee, Oversight and Investigations Subcommittee appreciates your participation in the hearing entitled, "HUD's Proposed RESPA Rule" held on September 16, 2008. Please provide written responses to the follow-up questions below within 30 days to be submitted as part of the hearing record.

Mr. MARC SAVITT – National Association of Mortgage Brokers (NAMB)

1. Should compensation for each actor in the mortgage settlement process (e.g. realtor, broker, settlement agent, lender) be disclosed? Is the proposed RESPA rule for disclosure of yield spread premiums sufficient to serve this purpose and is it beneficial to consumers? What other concerns, if any, do you have about yield spread premiums or the disclosure of yield spread premiums under RESPA?

Answer: Disclosure should be treated equally among distribution channels. Because consumers are largely unaware of, and indifferent to, the technical distinctions drawn between the originators with whom they are dealing, it is imperative that consumers be given the same information about the mortgage transaction regardless of the type of originator involved.

To serve consumers' interests effectively, regulatory initiatives relating to mortgage originators must address the mortgage market as it is today, not as it existed a generation ago. This means acknowledging the convergence of the roles of brokers, banks, and lenders; and applying rules equally to all of these originators.

It is now common for mortgage companies to act in multiple capacities. Even within a single transaction, the role in which a company may act may change during the application and processing functions from a lender to a broker, and back again, depending on circumstances. In addition, since HUD authorized affiliated business arrangements ("AfBAs"), many entities in the mortgage industry have established such relationships with developers, builders, real estate agents, and title companies, thus further confusing traditional roles and responsibilities.

NAMB has serious concerns about the Proposed Rule's inequitable disclosure of yield Spread premiums ("YSP"). The Proposed Rule reclassifies YSP as a credit to the borrower. The practical effect of this change is to put mortgage brokers at a competitive disadvantage by imposing asymmetrical disclosure obligations among originators receiving comparable compensation. Recharacterizing YSP as a credit to the borrower also invites gamesmanship by competing originators, which may exacerbate rather than eliminate confusion among consumers when shopping for a mortgage loan. The Proposed Rule also would at times require the reported credit to be negative, a result which almost certainly would increase confusion among borrowers.

The Proposed Rule perpetuates the inequity between broker and lender transactions, as regulated under RESPA. Despite the fact that our mortgage market has evolved and originators' roles have converged under the "originate to distribute" model, the Proposed Rule maintains, and even accentuates, an artificial difference between broker transactions (disclosure of YSP) and lender transactions (no disclosure of similar indirect compensation). As we have outlined in detail above, the era of clear differentiation between competitors in the mortgage market is over. The fact that this arbitrary distinction is perpetuated in the new GFE represents a fatal flaw in the Proposed Rule.

2. Should the GFE and the HUD-1 be the same format? If so, why? If not, why not?

Answer: Yes, NAMB believes that the HUD-1 and GFE should mirror each other and promote clarity, understanding, and ease of use for consumers. However, because the proposed GFE, at four pages, is less user-friendly than

the current version, mirroring the HUD-1 after the proposed document will not make it easier for consumers to understand and use.

It is critical that consumers be able to compare their costs "apples to apples", so to speak, when reviewing the settlement costs from several mortgage providers or when comparing the final settlement costs against the initial proposal. The well-documented 2004 study by the Federal Trade Commission of HUD's proposed GFE form showed that many consumers would choose a higher cost loan from a direct lender over a mortgage broker loan because of they were confused by HUD's proposed format for YSP disclosure. To leave YSP in the current form only promotes confusion for the consumer and is counter productive to HUD's stated goal for clarity.

NAMB strongly advocates ensuring that the GFE, HUD-1, and any other documents developed by HUD under RESPA impose symmetrical disclosure obligations on all mortgage loan originators. Failure to do so would deprive consumers of important information, and compromise their economic interests by impeding competition among originators.

3. What specific suggestions do you have as to how the RESPA rule issued by HUD and the TILA rule issued by the Federal Reserve should be harmonized?

Answer: The Federal Reserve's Proposed Rule addressed the YSP in a manner that was, admittedly so, confusing to the consumer and reduced competition in the marketplace. In its comment letter, NAMB stated that the manner in which the Federal Reserve was requiring such disclosure of the YSP was confusing to the consumer. NAMB explained that by applying such disclosures to mortgage brokers but not to creditors' employees who originate loans, would reduce competition in the market and harm consumers. NAMB explained that disclosing a brokers' compensation would cause consumers to believe, erroneously, that a loan arranged by a broker would cost more than a loan originated by a loan officer. The Federal Trade Commission commented and cited its published report of consumer testing on mortgage broker compensation disclosures, and stated that focusing consumers' attention on the amount of the broker's compensation could confuse consumers and, under some circumstances, lead them to select a

more expensive loan. The Federal Reserve considered these comments, conducted consumer testing and withdrew the proposal relating to YSP. In its final rule, the Board stated it is "concerned that the proposed agreement and disclosures would confuse consumers and undermine their decision-making rather than improve it." [1] The Board recognized that such disclosure of the YSP, as proposed, would not serve in the consumers' interest and in fact, would further confuse the consumer. HUD's Proposed RESPA rule requires disclosure of the YSP that will produce the same or a similar result as the Board's proposed YSP disclosure.

The Federal Reserve stated that they will "continue to explore available options to address potential unfairness associated with originator compensation arrangements such as YSP. As the Board comprehensively reviews Regulation Z, it will continue to consider whether disclosures or other approaches could effectively remedy this potential unfairness without imposing unintended consequences."[2] NAMB believes HUD, at a minimum, should take the same approach with its RESPA rule.

HUD's Proposed Rule states, "As HUD moves forward to finalize this, rule, it will continue to work with the Board to make the respective rules consistent, comprehensive, and complementary."[3] Noting that intention, however, is of no consequence. Just as the Proposed Rule must explain how it relates to existing law, it must explain how it relates to the Federal Reserve Board's proposed amendments to Regulation Z. The APA requires as much, as does sound rulemaking.

The Proposed Rule also does not address the Risk-Based Pricing regulations[4] the Federal Reserve Board and FTC recently proposed pursuant to the "Fair and Accurate Credit Transactions Act of 2003," or "FACT Act."[5]

The FACT Act, which amended the Fair Credit Reporting Act ("FCRA"), created a new disclosure requirement – the Risk-Based Pricing Notice ("RBP"). The RBP must be given to the consumer when the credit report affects pricing or other terms of the credit product. Specifically, the statute

[1] 73 Fed. Reg. at 44,563 .
[2] 73 Fed. Reg. at 44,565.
[3] 73 Fed. Reg. at 14,034.
[4] Federal Reserve Board and FTC, *Fair Credit Reporting Risk-Based Pricing Regulations*, 73 Fed. Reg. 28,966 (May 19, 2008).
[5] Public Law 108-159.

says that the RBP must be given to a consumer when credit is extended on "material terms that are materially less favorable than the most favorable terms available" to a "substantial proportion" of that creditor's other customers. The notice may generally be provided at application, communication of an offer of credit, or when the credit is granted (closing for real estate transactions), which would allow lenders and brokers to provide a generic notice to all applicants at the time of application. But the FACT Act allows the Federal Reserve Board and FTC to specify the timing of providing the notice after the credit report has been used to set the rates and terms of the offer, thereby making the notice much more consumer-specific. Those requirements could affect RESPA regulations in numerous ways, none of which are addressed by the Proposed Rule. It is essential that the Proposed Rule assess their impact before finalizing still more mandated disclosures.

HUD should seek public comments on the interaction between its proposal, the final amendments to Regulation Z and the pending RBP regulations. HUD should also work with the Board as it considers additional disclosures to TILA. Further, input from the parties who must comply with, and hope to benefit from, HUD's Proposed Rule is certain to improve any final regulation.

4. What is your estimate of the economic impact of the proposed RESPA rule on the mortgage broker industry and explain the basis of your estimate.

Answer: The economic impact will be illustrated through the shrinking of mortgage brokers thereby reducing origination channels and options for consumers. The December 2007 study by Richard Todd of the Federal Reserve Bank of Minneapolis and Professor Morris Kleiner of the Hubert Humphrey Institute of Public Affairs at the University of Minnesota also notes the beneficial role which mortgage brokers can have. Furthermore, that study also presents data which strongly suggests that, by enhancing competition, mortgage brokers help consumers obtain better and more appropriate mortgages at more favorable prices. That study, which was released as the Proposed Rule was being finalized and is thus not cited by the Rule, observed:

> [B]rokers can make the complicated task of shopping and applying for the increasingly wide array of mortgage products more manageable and efficient for borrowers and

> lenders alike. Millions of households, including many affluent and sophisticated consumers, have arranged mortgages through brokers, frequently more than once. It seems likely that many if not most of them found value in the brokers' services, which is what we would expect in honest, competitive markets.[6]

The study further observed that in those states which imposed particularly burdensome regulations on mortgage brokers through significant bonding requirements, the number of brokers was relatively low. In turn, the study established that the lower number of brokers was associated with "negative consequences for many consumers," including "higher foreclosure rates, and a greater percentage of high-interest-rate mortgages."[7] Although the study refrained from concluding a causal link between the number of mortgage brokers in a market and favorable conditions for consumers, the study did conclude a clear statistical correlation existed between the two. Moreover, that correlation comports with basic economic axioms, as well as common sense: if consumers have greater choice among more vendors, and are given the tools to make informed choices about the relative merits of the products those vendors offer, consumers are certain to benefit.

Through enhanced competition, markets expand, costs decline, and service improves—developments which benefit the general public. NAMB strongly supports measures which empower consumers to select mortgages based upon their own assessment of the comparative price, most appropriate product, and highest quality service (regardless of whether such a mortgage is obtained with the assistance of a broker).

5. Should the proposed RESPA rule allow real estate industry participants to offer incentives to create "one-stop shopping" for borrowers? Are certain industry segments hurt by the bundling of services? If bundling is not allowed, do you have other suggestions about how to reduce the costs associated with real estate settlements?

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[6] Broker Regulations Analysis at 2-3.
[7] Id. at 1.

Answer: Generally, NAMB believes that mortgage brokers, as small businesses, can be greatly disadvantaged by any "regulatory driven packaging" (as opposed to market driven packaging) of settlement services. Mortgage brokers, as small businesses, do not have the bargaining power to enter into volume-based discounts with third party settlement service providers as do larger entities. Depending on how the packing is proposed, if proposed like the previous HUD RESPA rule (2002), brokers would not be able to compete with the larger entities and will be forced to cease the transaction of business, become an agent for one lender or two, utilizing their packages or utilize the good faith estimate approach, which could also disadvantage mortgage brokers. This would force mortgage brokers to lose their autonomy, which is beneficial to consumers in the form of more consumer choice. This impact will be passed through to the consumers in the form of higher costs and less consumer choice. Additionally, the packaging of settlement services is occurring today. Thus, the removal of regulatory barriers is not necessary to allow packaging of settlement services.

6. Are there other regulatory or legislative changes needed for RESPA?

Answer:
1)Evaluate current, proposed, and pending disclosure requirements for originator compensation and coordinate with other agencies to develop effective disclosures that best serve consumer interests

The multiple broker compensation disclosures already mandated by current law and industry practice underscore the importance of reducing complexity and avoiding information overload. In addition to current broker compensation disclosures in both the GFE and HUD-1, the Federal Reserve Board has proposed extensive new disclosures pursuant to TILA. In addition, the Federal Reserve Board and the FTC have issued proposed regulations detailing new RBP disclosure requirements under the FACT Act. All 50 states also regulate brokers and their compensation in various respects. Industry practice and lender requirements mandate still further disclosures.

NAMB requests HUD to evaluate how the Proposed Rule's mortgage broker compensation disclosures would relate to each of the other currently mandated or contemplated disclosures, explain its findings,

and determine how additional disclosures would achieve its goal of informing consumers while limiting "complexity and information overload."

2). Implement the enhanced disclosure forms developed by the FTC

Over the course of several years, the FTC, the federal agency with primary responsibility for consumer protection, has conducted research into the efficacy of proposed disclosures of mortgage broker compensation and their effect on consumer decisions and market outcomes. The FTC has presented its findings in two separate reports totaling over 400 pages. The prototype disclosure forms developed by the FTC based on its research include prominent legends in large typeface which expressly advise borrowers that mortgage originators, including both brokers and lenders, do not represent borrowers, and thus the "lender or broker providing this loan is not necessarily shopping on your behalf or providing you with the lowest cost loan." The legend also encourages borrowers, in all caps, to "COMPARISON SHOP TO FIND THE BEST DEAL."

NAMB strongly urges HUD to adopt language from the FTC prototype disclosure forms instead of implementing the Proposed Rule's provisions on broker compensation. The FTC forms have been thoroughly tested, and they are a less burdensome and more effective means of addressing the policy concerns raised by the Proposed Rule. Also, as the FTC has explained, the prototype forms do not create anti-broker bias that can impede competition and lead consumers to make choices that are not in their best interests.

3). Apply all applicable regulations to all originators on the same terms

The Proposed Rule fails to implement the principle, enunciated in the Department of Treasury's Blueprint for a Modernized Financial Regulatory Structure and affirmed by independent academic researchers, that "Federal mortgage lending laws should ensure adequate consumer protection for all types of mortgage originators"[8] and "that all mortgage brokers, loan officers, and mortgage originators play by the same rules."[9]

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[8] Treasury Blueprint at 81.

[9] Harvard Mortgage Study at vi.

NAMB strongly urges HUD to revise the Proposed Rule so that all regulations treat all originators similarly. Likewise, any disclosure forms developed under those regulations must require the same disclosures from all originators. Towards that end, NAMB has developed a model disclosure form ("Model Form"), appended hereto as Exhibit A, which provides symmetrical disclosure of originator compensation regardless of channel. NAMB recommends that HUD examine the Model Form, and adopt its provisions to facilitate the Proposed Rule's stated goal of facilitating comparative shopping.

The Model Form is preferable to the proposed GFE form on several grounds. Not only does it remedy the disparity among originator disclosures, it also more closely mirrors the current HUD-1, thus facilitating comparative shopping; it does not create groupings of disclosures that later must be broken out; and it is one page rather than four, making it much more user friendly. (Other items not noted in the Model Form could still be addressed in the required HUD pamphlet.)

The Proposed Rule fleetingly acknowledges the policy merits of requiring similar disclosures by all originators, but cites practical impediments to determining that figure for lenders. However, quantifying a lender's compensation on a loan sold well into the future is both unnecessary because it does not affect the price paid by the borrower. What is relevant is the incremental cost to the consumer assessed at the time of closing that is attributable to the differential between the loan rate and the wholesale rate. And that figure, unlike the subsequent amount which may be earned upon sale of the loan at some undetermined date in the future, can be computed and disclosed prior to closing. HUD should specify how that computation should be done, and require disclosure of the resulting figure, just as the Proposed Rule would do with respect to YSP.

4) Specific Proposed Revisions to the GFE

1. The definition of mortgage broker should be further expanded to capture any originator that sells loans servicing released within six months of origination. Doing so does not present insuperable practical problems. Where loans are sold prior to or shortly after origination, the SRP and payments created by AfBA relationships are known early in the transaction because it is used to establish the closing rate.

2. The term "service charge" should not be used on the proposed GFE (page two, block one). Use of that term presents potential problems under state law, as some states expressly prohibit originators from imposing a "service charge," and others impose taxes on services. Also, use of the term may complicate application of IRS regulations that allow consumers to deduct broker origination fees because characterizing such fees as a "service charge" could affect their deductibility under IRS regulations. A possible alternative could be "origination charges," which would also correspond to the reference to "Adjusted Origination Charges."

3. YSP should not be recharacterized as a credit to borrower. The practical effect of this change is to put mortgage brokers at a competitive disadvantage by imposing asymmetrical disclosure obligations among originators receiving comparable compensation. Recharacterizing YSP as a credit to borrower also may invite gamesmanship by competing originators that may create, rather than eliminate, confusion among consumers. The Proposed Rule also, as it acknowledges,[10] would at times require the reported credit to be negative, a result which almost certainly would increase confusion among borrowers. The box at the top of page two is confusing and counterproductive, and should be deleted. Instead, originator compensation should be reported clearly both at the bottom of page one, and as a separate, and prominent, line item on page two.

4. The introductory language on page one of the revised GFE is too vague. The revised form, appended to the Proposed Rule, reads: "The interest rate for this GFE will be available until ____." As a general matter, it is meaningless to quote a rate prior to final application. Nonetheless, if a reference to the rate must be included in the revised GFE, a possible alternative to the proposed language could be: "The interest rate quoted on this GFE is ___. This rate is not guaranteed. Until it is locked, this rate will float with the market and can change without notice."

5. The Proposed Rule would provide that the revised GFE include a summary of the key terms of the loan, including the initial loan amount, the loan term, the initial interest rate, the initial monthly

[10] 73 Fed. Reg. at 14,048.

payment, and the rate lock period. NAMB recommends that additional costs be included among the loan details identified in the GFE. Specifically, NAMB believes that consumers would be well served by the inclusion of certain additional monthly expenses specific to the property, such as homeowners association dues, if applicable.

6. The period during which the GFE terms are available to the borrower (i.e., "ten business days") is too long. A more workable period would be "ten calendar days."

7. The Proposed Rule does not require that settlement service providers be named on the GFE. In addition, the Proposed Rule impedes transparency to the consumer by permitting the consolidation of fee categories. All settlement service charges should be itemized, and the names of the settlement service providers should be specified

8. Page four, line one of the proposed GFE reads "...you may need to pay other annual charges to keep your property." NAMB recommends that the language be revised to read as follows: "...you will need to pay other annual charges to keep your property."

9. NAMB recommends that the disclosure found at the bottom of page four of the proposed GFE regarding the lenders' additional compensation be presented as part of a more prominent disclosure, adapted from the language developed by the FTC, describing the relationship of loan originators to the borrower, highlighting the importance of comparative shopping, alerting the borrowers that they are the only ones who can conduct that comparative shopping on their own behalf, and explaining the interplay between mortgage rates, originator compensation, and closing costs.

RESPRO
Real Estate Services Providers Council, Inc.

Answers to Questions
By the House Committee on Financial Services
Subcommittee on Oversight & Investigations

Hearing entitled "*HUD's Proposed RESPA Rule*," September 16, 2008

By David Stevens
President-Chief Operating Officer, Long and Foster Companies

1. **Should compensation for each actor in the mortgage settlement process (e.g., realtor, broker, settlement agent, lender) be disclosed? Is the proposed RESPA rule for disclosure of yield spread premiums sufficient to serve this purpose and is it beneficial to consumers? What other concerns, if any, do you have about yield spread premiums or the disclosure of yield spread premiums under RESPA?**

   RESPRO® believes that each actor who is providing and is accountable for each separate service should disclose the fee it is charging the borrower. This is the essential purpose of the HUD-1 Settlement Statement. However, we do not believe that it is necessary to disclose the compensation arrangements that providers may have with each other; to the contrary, we believe that this additional information would prevent apple to apple comparisons and ultimately comparison shopping by consumers. For example, we do not believe that it is necessary to require providers to disclose on the HUD-1, as HUD's final RESPA rule ultimately required, how much of the title insurance premium goes to the title agency and how much goes to the title underwriter. The borrower ultimately wants to know the total cost so that he/she can easily compare it to the costs of other providers.

   RESPRO® has not taken a position on how yield spread premiums should be disclosed.

2. **Should the GFE and the HUD-1 be in the same format? If so, why? If not, why not?**

   RESPRO® applauds HUD's efforts to make the GFE be more comparable to the HUD-1 so that consumers can better track the disclosures and item numbers used on the GFE. Identical formats, however, would not be possible since there is information on the HUD-1 (e.g., real estate brokerage commissions and fees; costs to be paid by sellers) that do not appear on the GFE.

3. **What specific suggestions do you have as to how the RESPA rule issued by HUD and the TILA rule issued by the Federal Reserve should be harmonized?**

As we stated in our June 2008 comments to HUD, RESPRO® believes that HUD and the Federal Reserve Board should work together to develop a single mortgage disclosure document, rather than requiring separate TILA and RESPA disclosures.

The Good Faith Estimate and the HUD-1 Settlement Statement (the RESPA disclosures) were intended to provide consumers the estimated and then actual settlement costs. The TILA disclosure was intended to provide consumers a disclosure of the loan terms. These purposes overlap to begin with, and HUD's final GFE and HUD-1 exacerbate the problem by containing loan terms that are duplicative and/or inconsistent with the current TILA disclosure. It is noteworthy that the Federal Reserve Board itself strongly recommended in its comments to HUD during the rulemaking process that HUD work with it to harmonize the two rules, and if possible, to develop a single disclosure form that would prevent consumers from having to consult different and sometime inconsistent disclosures to get a full picture of the settlement and loan terms.

In addition, the Federal Reserve Board currently is considering modifications to the TILA disclosure that would be implemented at a different point of time than HUD's final RESPA disclosures. Therefore, mortgage lenders will need to invest in the software and training necessary to implement the new RESPA disclosures, and then subsequently invest in additional software and training to implement a new TILA disclosure. These are costs that serve no purpose for the consumer and impose unneeded burdens on the mortgage industry during a fragile economic time.

4. **What is your estimate of the economic impact of the proposed RESPA rule on the "diversified" or "affiliated" real estate companies and explain the basis of your estimate.**

As I stated in my testimony, the proposed RESPA rule essentially would have prohibited diversified firms like Long and Foster from offering consumers positive incentives that have enabled us to assure that our customers get to closing on time and that have resulted in substantial savings and/or better service to them. While the final rule has been modified to address many of the concerns of diversified real estate brokerage firms, its language is complex and it still prevents homebuilders from offering any incentives that involve the use of their affiliated mortgage, title, or settlement service companies.

In the Regulatory Impact Analyses accompanying its proposed and final rules, HUD did not provide any empirical evidence supporting these restrictions and ignored empirical studies that conclusively show that affiliated businesses offer settlement service pricing that is no more than (and may be less than) those of unaffiliated companies.

The most recent economic study on the costs of affiliated services vs. unaffiliated services involved an independent analysis of over 2200 HUD-1 Settlement Statements from transactions conducted in nine states (Alabama, Illinois, Maryland, Michigan, Minnesota, North Carolina, Ohio, South Carolina and Virginia) in 2003 and 2005. The study concluded that title premiums and title-related settlement closing charges are not higher when affiliated business arrangements are involved compared to when they are

not. The CapAnalysis Study reached the same conclusion as a 1994 study performed by the national economic research firm of Lexecon, Inc., which found that title and title-related services for transactions performed by affiliated title companies in seven states – Florida, Minnesota, Tennessee, Wisconsin, Mississippi, Pennsylvania, and California – were competitive with those provided by unaffiliated title companies.

5. Should the proposed RESPA rule allow real estate industry participants to offer incentives to create "one-stop shopping" for borrowers? Are certain industry segments hurt by the bundling of services? If bundling is not allowed, do you have other suggestions about how to reduce the costs associated with real estate settlements?

We believe that HUD should allow incentives for one-stop shopping as long as the incentives are optional and are not compensated by increased costs elsewhere in the transaction. This is what HUD's current RESPA regulations have provided for 16 years. As I stated above, HUD provided no empirical evidence to support its proposed and final changes to this regulation. Instead, it heavily relied on anecdotal information involving incentives that either were <u>not</u> optional or that were compensated by increased costs elsewhere in the transaction – which violate current RESPA regulations and could be dealt with by more effective enforcement.

In fact, the changes to RESPA's rules regarding incentives were advocated not by <u>consumers</u>, but by <u>competitors</u> of affiliated businesses whose potential customers often prefer to use affiliated services because of the convenience, competitive costs, and greater accountability that they can provide. They also value the savings they can get from incentive programs -- as I stated in my testimony, a 2008 survey of home buyers conducted by Harris Interactive found that 77% of home buyers consider the biggest advantage of using one-stop shopping programs is saving money through discounted prices.

RESPA was enacted by Congress to prevent unnecessarily high settlement costs for <u>consumers</u>, not to protect segments of the industry from competition. As the Federal Trade Commission noted in its comments to HUD during the rulemaking process, these incentives are not anticompetitive and they can be beneficial to consumers. It is possible that some competitors may find it difficult to compete with a company who offers multiple services, convenience and accountability, but we do not believe that this is the type of harm which HUD or Congress needs to address.

In response to your question about how to reduce settlement costs, we believe that HUD's proposed and final rules would increase costs in many transactions restricting many consumer incentives offered today that result in substantial savings, and that this requirement should be withdrawn. In addition, HUD has required the mortgage industry to incur substantial costs to implement its new RESPA disclosures when it likely will have to incur additional costs to implement new TILA disclosures in the future – which ultimately will be borne by the consumer. This could have been avoided if HUD had

collaborated with the Federal Reserve Board to develop a uniform mortgage disclosure (see response to Question 3), and we still urge Congress to encourage HUD to do so.

Finally, I would like to clarify that the term "bundling" has been used in multiple contexts in the industry. At one point, it was used to refer to a concept presented by HUD in a 2002 proposed RESPA rule and in a 2004 final RESPA rule (withdrawn before publication) that is different from the "bundling" offered by diversified or affiliated companies. HUD's 2002 proposed rule and 2004 final rule would have provided an exemption from RESPA's referral fee prohibition for mortgage lenders that offered a total mortgage and settlement service "package" or "bundle" at a single guaranteed price. RESPRO® supported its withdrawal in favor of a RESPA rule that would simplify the Good Faith Estimate and make it more comparable to the HUD-1.

6. Are there other legislative or regulatory changes needed for RESPA?

See my responses above concerning the need for HUD to collaborate with the Federal Reserve Board on a uniform mortgage disclosure.

RESPRO® is aware that HUD plans to submit proposed legislation to Congress in 2009 that would allow it to impose additional penalties under RESPA, including civil money penalties and "fair and equitable relief" (e.g., disgorgement). RESPRO® has consistently expressed its concern about illegal kickbacks in the marketplace by both unaffiliated and affiliated businesses, and has consistently supported more RESPA enforcement by federal and state regulators. However, HUD often has not provided clear guidance under the law over the years and often has provided confusing and inconsistent guidance.

For example, HUD has attempted in a 1996 Policy Statement to provide guidance on how joint ventures and marketing agreements should be structured under RESPA, but the guidance in the Statement is difficult to understand. Yet HUD, unlike most other federal agencies, has no program whereby advisory opinions or "no action" letters can be obtained by companies like Long and Foster that sincerely want to assure that their programs comply with RESPA.

Therefore, we believe that before Congress acts on HUD's forthcoming proposals, it should assure that HUD creates a system under which settlement service providers can obtain more consistent more clear regulatory guidance under RESPA, and that it also should preclude windfall remedies that now occur from technical violations that do not result in any consumer injury. Moreover, if such remedies are to be provided, Congress should establish a clear procedures and adequate review process for the imposition of such penalties and orders

Pulte Mortgage

November 6, 2008

VIA FACSIMILE (202-225-4254)

Committee on Financial Services
ATTN: Terrie Allison
U.S. House of Representatives
3039 Rayburn House Office Building
Washington, DC 20515

Re: September 16, 2008 Hearing on HUD's Proposed RESPA Rule

Dear Ms. Allison:

I write in response to the October 8, 2008 letter from Thomas G. Duncan, General Counsel of the Subcommittee on Oversight and Investigations, concerning the September 16, 2008 hearing where I testified on behalf of the National Association of Homebuilders. In his letter, Mr. Duncan requested that I provide corrections to the hearing transcript and that I respond to six questions submitted by Chairman Watt. I have no corrections to the transcript.

My responses to the questions follow.

1. **Should compensation for each actor in the mortgage settlement process (e.g. realtor, broker, settlement agent, lender) be disclosed? Is the proposed RESPA rule for disclosure of yield spread premiums sufficient to serve this purpose and is it beneficial to consumers? What other concerns, if any do you have about yield spread premiums or the disclosure of yield spread premiums under RESPA?**

Response:

The compensation of the entities involved in the mortgage settlement process should be disclosed, so long as the requirement does not include compensation from secondary market transactions. Secondary market income is too difficult to predict with certainty at the time of closing. Moreover, secondary market transactions are probably outside RESPA's regulatory scope, raising the likelihood that any such effort to regulate secondary market transactions through disclosure would be challenged in a court. While we agree that yield spread premiums should be disclosed to consumers, the proposed rule's approach to the disclosure is likely to create confusion for consumers for at least two reasons. First, the proposed GFE combines the origination fee paid to the lender with the income to the broker in one line item. A better approach would be to show each party's income separately, because mortgage brokers (who provide origination services and assist the consumer in shopping for a loan, but do not actually fund the loan) and mortgage lenders (who fund loans) provide distinctly different services. Second, the characterization of a yield spread premium as a credit to the borrower may further confuse consumers. While we support

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disclosure of the yield spread premium in the good faith estimate, we believe that it should be disclosed as a payment by the lender to the broker.

2. Should the GFE and the HUD-1 be the same format? If so, why? If not, why not?

Response:

Yes, the formats of the GFE and HUD-1 should be harmonized. Doing so would allow the consumer easily to compare the two documents, creating certainty and eliminating the need for redundant disclosures and other protections. The proposed four-page GFE falls short of the goal of making the GFE and HUD-1 correspond. In the current proposal, HUD found it necessary to propose a 45-minute "closing script" to be read by the closing agent and signed by the borrower, in an attempt to reconcile the proposed GFE and HUD-1.

3. What specific suggestions do you have as to how the RESPA rule issued by HUD and the TILA rule issued by the Federal Reserve should be harmonized?

Response:

We offer the following specific suggestions regarding how the RESPA rules and the TILA rule should be harmonized.

First, the Federal Reserve Board and HUD should engage in joint, comprehensive rulemaking to create a simplified, seamless set of disclosures that meet the requirements of the federal Truth in Lending Act and the RESPA for consumers. With this goal in mind, we support the form developed by the Mortgage Bankers Association, with the first page displaying the settlement costs and the second page displaying the costs of credit for consumer's mortgage. A copy of the form is attached as Exhibit A hereto.

Alternatively, if HUD goes forward with rule-making independently, it should adopt a GFE form and corresponding HUD-1 Settlement Statement proposed by the MBA. A copy of this form is attached as Exhibit B. These forms properly distinguish between "Lender Origination Charges" and "Mortgage Broker Origination Charges" and disclose the yield spread premium as "Amounts Paid by Lender to Broker on your behalf." The MBA's proposed GFE format also has the advantage of being easily reconcilable to its proposed HUD-1.

4. What is your estimate of the economic impact of the proposed RESPA rule on the homebuilder industry and explain the basis of your estimate.

Response:

The economic impact of the proposed RESPA rule, if adopted, would be substantial. Specifically, we would expect that homebuilders' affiliated lenders and title companies would incur substantial costs to retool, reprogram and train in order to adopt a new GFE application and the four-page GFE. The proposed changes are broad enough that large homebuilders and their captive mortgage lenders could spend hundreds of thousands of dollars each to implement the changes. Additionally, the 45-minute

closing script required under the proposed rule will likely raise closing costs by hundreds of dollars per transaction, given the amount of time necessary to prepare and read the script.

Even more significant than these generic changes, however, is the proposed change to the "required use" definition in RESPA's Regulation X. The change is specifically targeted at homebuilders and would prohibit them from offering incentives to buyers that use affiliated lenders and title companies. Over the last sixteen years, homebuilders have perfected an affiliated business model, based on existing regulations that permit affiliated business incentives. The affiliated business model today is mature, high-performing and customer-responsive. For HUD to tear down this model through implementation of its proposed change to the "required use" definition (the need for which is unsupported by the administrative record) would exact an unnecessary and material expense on an industry that is already challenged by current economic conditions.

The change to the "required use" definition would exact a unique and significant cost on our industry at a time when homebuilders and the nation cannot afford it. As I explained during the hearing, the unfortunate result of prohibiting incentives would be to lower homebuilders' capture rates (i.e., the rate that the builder successfully consolidates the sale with its affiliate lender), perhaps by 20 percent or more, and thereby destroy the values created through affiliated business synergies, which today are passed on to consumers in the form of incentives.

Accordingly, not only homebuilders would be affected, but consumers would lose too, under the new "required use" definition. New homebuyers would no longer be entitled to share – in the form of incentives -- the benefits that result from affiliated business synergies.

Accordingly, we would expect that implementation of the proposed "required use" definition to result in increased new home prices and lost deals. Homebuilders would incur increased overhead costs, including costs associated with the need to coordinate closings with a multitude of non-affiliate lenders, as well as the costs associated with closings that were delayed or even canceled, due to financings that fell through at the last minute after being placed with less-experienced or unreliable outside lenders.

5. **Should the proposed RESPA rule allow real estate industry participants to offer incentives to create "one-stop shopping" for borrowers? Are certain industry segments hurt by the bundling of services? If bundling is not allowed do you have other suggestions about how to reduce the costs associated with real estate settlements?**

Response:

The proposed rule should allow participants to offer one-stop shopping, so long as the requirement remains to itemize the individual costs. Consumers have long favored the convenience of one-stop shopping. Moreover, if RESPA reform is done correctly, consumers may benefit from efficiencies created through bundled services.

6. **Are there other regulatory or legislative changes needed for RESPA?**

Committee on Financial Services
November 6, 2008
Page Four

Response:

We suggest the following. First, we would emphasize that need for joint TILA/RESPA rulemaking and a comprehensive regulatory approach. In our view, this comprehensive approve would require that HUD and the Federal Reserve work together on a single disclosure approach.

Second, we believe that the residential mortgage lending system requires a single approach to disclosure and to regulation across the country. The current system, which allows for significant state-by-state variation, as well as variation among different types of lenders (banks versus thrifts versus state-licensed lenders) results in redundant, confusing and potentially contradictory disclosures and, in virtually all instances, increases transaction costs.

Third, we believe that the current regulatory and licensing system, notwithstanding recent improvements in the SAFE Act (which was part of the Housing and Economic Improvement Act of 2008), still provides an economic barrier of entry that is too low to weed out potential players that are financially unsound or irresponsible. Although licensing and education, as required under the SAFE Act, are a step in the right direction for the residential mortgage industry, requirements regarding capitalization or net worth should also be implemented.

On behalf of the National Association of Homebuilders and Pulte Homes, Inc., I thank you for the opportunity to share our views on these issues of great importance to our country.

Very truly yours,

Debra W. Still
President and Chief Executive Officer
Pulte Mortgage LLC

Enclosures
cc: National Association of Homebuilders

Exhibit A

Exhibit A

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT [Optional language is in brackets] PAGE 1

Combined Good Faith Estimate of Settlement Costs and Truth in Lending Act Disclosure

Lender Name and Address	Mortgage Broker Name and Address	File Number
Buyer/Borrower Name and Address	Property Address	Date GFE Provided

Loan Description

Proposed Mortgage Loan Amount $ ________ ☐ Conventional ☐ FHA ☐ VA ☐ FSA/RHS

About this Combined Good Faith Estimate of Settlement Costs and Truth in Lending Act Disclosure

This disclosure contains a Good Faith Estimate of your settlement costs on page 1 and Truth in Lending disclosures of your loan's terms and costs on page 2. These are estimates based on information you provided. If your loan is approved, the estimated amounts may change based upon conditions discovered by the Lender in underwriting, or, if, among other things, you request a change in the loan amount, term, type of loan or lock your interest rate at a different time or on different terms

Mortgage Loan Settlement Charges to Be Paid by You

The line numbers below correspond to the item numbers on the HUD-1 Settlement Statement you will receive at loan closing. You should compare this Disclosure with the HUD-1 Statement you receive at closing to determine whether any changes have occurred and the reason for any changes. Call your lender or mortgage broker with any questions

Prepaid Finance Charges of $________ are included in the Settlement Charges shown below and are marked with an †. Your Prepaid Finance Charges together with interest and other lender-required loan related charges you will pay after closing (such as mortgage insurance premiums, if applicable) are shown on your Truth in Lending Disclosure as the Finance Charge.

800. Lender Origination Charges† (Line 801 plus 802 plus 803 less 804) $ ________

- **801 Lender Charges** for loan origination and other Lender services $ ________
- **802 Discount Points** paid to reduce your interest rate ________% $ ________
- **803 Rate Lock** paid to lock in your interest rate ________% $ ________

  (If you lock in your rate at a different time or on different terms, the lock fee may change. See your Rate Lock Agreement for additional details.)
- **804 Lender Credit** for your choosing a higher interest rate ($ ________)

900. Mortgage Broker Origination Charges† (Line 901 less 902) $ ________

- **901 Total Broker Compensation** for Broker's services $ ________
- **902 Amounts Paid by Lender** to Broker on your behalf ($ ________)

Important Information When Using a Mortgage Broker. If you have agreed that the Lender may pay the Broker on your behalf part of the Total Broker Compensation (line 902), you will pay this amount through your loan's interest rate and monthly payment. Your Mortgage Broker is required to enter into a Mortgage Broker Fee Agreement with you, which you should review.

1000. Credit Report and Pre-Closing Appraisal and Inspection Charges $ ________

For credit reports, appraisals, property valuations, inspections, tax or flood determinations.

1100. Title and Closing Charges (Sum of lines 1101–1105) $ ________

- **1101 Title Charges** $ ________

  (Lender's title insurance, survey, title examination, notary services, abstract or title search, documentation preparation)
- **1102 Owner's Title Insurance** with title coverage of $ ________ $ ________
- **1103 Closing Agent** to attend closing† $ ________
- **1104 Services Required** by closing agent but not by Lender $ ________
- **1105 Closing Agent Services** required by Lender† $ ________

1200. Government Recording & Transfer Charges $ ________

1300. Items Required by Lender to be Paid in Advance (Sum of lines 1301–1306) $ ________

- **1301 Daily Interest Charges†** from the day of your settlement until the first day of your normal payment cycle, estimated at $ ________ per day for 30 days $ ________
- **1302 Taxes** $ ________
- **1303 Hazard Insurance Premium** $ ________
- **1304 Flood Insurance Premium** $ ________
- **1305 Mortgage Insurance Premium†** $ ________
- **1306 Other (Specify)** ________ $ ________

1400. Initial Escrow Deposit† for escrow account to pay taxes, insurance, and other charges $ ________

☐ Mortgage insurance premium reserves of $ ________ are included in this amount

1500. Other Mortgage Loan Settlement Charges† such as life-of-loan flood and tax services, lender's attorney's fees, wire transfer and other miscellaneous services not covered above $ ________

1600. Total Estimated Mortgage Loan Settlement Charges $ ________

1700. Mortgage Loan Settlement Charges to be Paid by Borrower at Settlements $ ________

(Line 1600 less 1701 less 1702 less 1703)

- **1701 Amounts Paid by Borrower Before Closing** ($ ________)
- **1702 Amounts from Lender or Mortgage Broker** ($ ________)
- **1703 Settlement Charges Paid by Seller** ($ ________)

Note: In a purchase transaction the amount you will pay at settlement will be affected by whether the seller has agreed to pay any of the settlement charges, by the amount of your down payment, and by the amount you have already paid as a deposit. Settlement charges paid by seller (line 1703) will appear on the HUD-1 Settlement Statement.

You are entitled to shop for a limited number of settlement services. Check with your lender about the services you may shop for. These services and their charges are included in your Mortgage Loan Settlement Charges shown on line 1700 above; if you shop for these services, however, these amounts may change.

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT [Optional language is in brackets] PAGE 2

Combined Good Faith Estimate of Settlement Costs and Truth in Lending Act Disclosure

Lender Name and Address	Mortgage Broker Name and Address	File Number
Buyer/Borrower Name and Address	Property Address	Date GFE Provided

Loan Description

Proposed Mortgage Loan Amount $ ________ ☐ Conventional ☐ FHA ☐ VA ☐ FSA/RHS

About this Combined Good Faith Estimate of Settlement Costs and Truth in Lending Act Disclosure
This disclosure contains a Good Faith Estimate of your settlement costs on page 1 and Truth in Lending disclosures of your loan's terms and costs on page 2. These are estimates based on information you provided If your loan is approved, the estimated amounts may change based upon conditions discovered by the Lender in underwriting, or, if, among other things, you request a change in the loan amount, term, type of loan or lock your interest rate at a different time or on different terms.

Annual Percentage Rate	Finance Charge	Amount Financed	Total of Payments
The cost of your loan as a yearly rate including interest as shown in the schedule below and other finance charges	The dollar amount the loan will cost you including Prepaid Finance Charges shown on page 1	Your Loan Amount less the Prepaid Finance Charges shown on page 1	The amount you will have paid after you have made all payments as scheduled
________ %	$ ________	$ ________	$ ________

Schedule of Interest Rates, Balances and Payments. Your loan has a term of ______ years, repayable as follows

Interest Rate	Beginning Principal Balance	Number of Payments	Amount of Payment	Payments Due Monthly Beginning

Payment Increases. If checked below, your loan has features that may cause your payments to increase. Consider carefully whether you can afford to make the higher payments. Do not assume that you will be able to refinance to lower your payments.

☐ **Adjustable Rate:** Your loan contains an adjustable rate feature. See the Truth in Lending Act disclosures provided to you earlier about your adjustable rate feature If the index used to adjust your interest rate increases, your actual interest rates and payments may be higher than shown above but your interest rate will not increase above ______ % and your payments will not increase above $ ______.

☐ **Interest Only:** The initial monthly payments cover only the interest on your loan amount If you pay only interest due, after a certain period of time, your monthly payment will increase because you must pay back principal and interest

☐ **Negative Amortization:** You may be allowed to make payments on your loan that do not cover all of the interest owed. Unpaid interest owed will be added to your principal balance, increasing the amount that you must repay, but your principal balance will not increase above $ ______

☐ **Balloon Payment:** Your loan must be paid off in one large final payoff payment of up to $ ______ after ______ years.

☐ **Demand Feature:** The entire amount owed on this loan is payable on demand This means that the lender may require you to pay off your loan in full at any time All disclosures are based on an assumed maturity of one year.

Mortgage Insurance.
☐ You will be required to pay the cost of mortgage insurance for your loan. Any amounts you paid at or before closing are disclosed on page 1 and any costs you will pay after closing are included in the payments shown above.
[ ] You will not be required to pay mortgage insurance for your loan

Payments for Taxes and Insurance. The payments shown above do not include amounts you will pay for real estate taxes and hazard insurance, estimated to be an additional $ ______ per month. This amount is subject to change throughout the term of the loan

☐ **Your loan provides** for an escrow account from which the lender will pay your taxes and insurance. Page 1 shows your initial escrow deposit Monthly escrow payments will be required You will receive an escrow account statement no later than 45 days after settlement

☐ **Your loan does not provide** for an escrow account. You are responsible for paying taxes and insurance when due.

Prepayment.
☐ Your loan has a prepayment charge. If you pay off during the first [time period], you may have to pay a charge of up to $ ______
☐ Your loan has no prepayment charge. If you pay off early, you will not have to pay a prepayment charge.

Hazard and Flood Insurance. You may obtain the required insurance from anyone you want that is acceptable to the lender

Late Charge. If a payment is late, you will be charged $ ______.

Security. If you obtain this loan, the lender will have a mortgage on your home. You could lose your home, and any money you have put into it, if you do not meet your obligations under the mortgage. You are not required to obtain this loan merely because you have received these disclosures or have signed a loan application

Assumption. Someone buying your house:
☐ **may, subject to conditions, be allowed** to assume the remainder of your mortgage on the original terms
☐ **will not be allowed** to assume the remainder of your mortgage on the original terms

Exhibit B

Exhibit]

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT [Optional language is in brackets] PAGE 1

Combined HUD-1 Statement of Settlement Costs and Final Truth in Lending Act Disclosure

Lender Name and Address		Mortgage Broker Name and Address	
Buyer/Borrower Name and Address		Seller Name and Address	
Settlement Agent		Property Address	
Settlement Date	Loan Number	File Number	MI Number

Loan Description

Proposed Mortgage Loan Amount $ __________ ☐ Conventional ☐ FHA ☐ VA ☐ FSA/RHS

About this Combined HUD-1 Statement of Settlement Costs and Truth in Lending Act Disclosure

This disclosure contains a summary of the borrower's and seller's transaction on page 1, your settlement costs on page 2 and the final Truth in Lending Act disclosures of your loan's terms and costs on page 3 You can compare the estimated settlement costs on your Combined Good Faith Estimate of Settlement Costs and Truth in Lending Act Disclosure provided to you earlier to the final settlement costs on page 2.

A. Summary of Borrower's Transaction	**B. Summary of Seller's Transaction**
100. Gross Amount Due from Borrower	**400. Gross Amount Due to Seller**
101 Contract Sales Price	401 Contract sales price
102 Personal Property	402. Personal property
103 Net Settlement Charges to be Paid by Borrower (line 1700)	403.
104	404
105.	405.
Adjustments for items paid by seller in advance	**Adjustments for items paid by seller in advance**
106 City/town Taxes to	406 City/town taxes to
107. County Taxes to	407. County Taxes to
108. Assessments to	408. Assessments to
109	409.
110.	410.
111.	411
112.	412.
120 Gross Amount Due from Borrower	**420. Gross Amount Due to Seller**
200. Amounts Paid by or on behalf of Borrower	**500. Reduction in Amount Due to Seller**
201. Deposit or earnest money	501. Excess deposit (see instructions)
202. Principal amount of new loan(s)	502. Net Settlement Charges to be Paid by Seller (line 1700)
203 Existing loan(s) taken subject to	503. Existing loan(s) taken subject to
204.	504. Payoff of first mortgage loan
205.	505. Payoff of second mortgage loan
206	506.
207	507.
208.	508.
209	509.
Adjustments for items unpaid by seller	**Adjustments for items unpaid by seller**
210. City/town taxes to	510. City/town taxes to
211 County taxes to	511 County taxes to
212. Assessments to	512. Assessments to
213	513.
214	514.
215.	515
216.	516.
217	517
218.	518
219.	519
220 Total Paid By/For Borrower	**520. Total Reduction Amount Due Seller**
300. Cash at Settlement From/To Borrower	**600 Cash at Settlement To/From Seller**
301. Gross Amount Due from Borrower (line 120)	**601 Gross Amount Due to Seller (line 420)**
302. Less Amounts paid By/For Borrower (line 220)	602. Less Reductions in Amount Due Seller (line 520)
303. Cash ( ) From ( ) To Borrower	603 Cash ( ) To ( ) From Seller

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT [Optional language is in brackets] PAGE 2

Combined HUD-1 Statement of Settlement Costs and Final Truth in Lending Act Disclosure

Lender Name and Address	Mortgage Broker Name and Address
Buyer/Borrower Name and Address	**Property Address**

C. Settlement Charges

Note: Prepaid Finance Charges of $______ are included in the Settlement Charges shown below and are marked with an † Your Prepaid Finance Charges together with interest and other lender-required loan related charges you will pay after closing (such as mortgage insurance premiums, if applicable) are shown on your Truth in Lending Disclosure as the Finance Charge.

C-1. Real Estate Sale Settlement Charges	Column A Paid From Borrower's Funds at Settlement	Column B Paid From Seller's Funds at Settlement
700. Total Real Estate Commission — sales price $ ______ at ______% A $ ______		
Division of Commission in 700 is as follows:		
701. $ ______ to ______		
702. $ ______ to ______		
703. Real Estate Commission on line 700 paid at settlement	$ ______	$ ______
704. Other (specify) ______	$ ______	$ ______
C-2. Other Charges for Transactions Not Required by Broker or Lender		
750. Borrower's Attorney's Fee	$ ______	$ ______
751. Other (specify) ______	$ ______	$ ______
C-3. Mortgage Loan Settlement Charges to Be Paid by You		
800. Lender Origination Charges† (Line 801 plus 802 plus 803 less 804)	$ ______	$ ______
801. Lender Charges for loan origination and other Lender services $ ______		
802. Discount Points paid to reduce your interest rate ______% / $ ______		
803. Rate Lock paid to lock in your interest rate ______% / $ ______		
804. Lender Credit for your choosing a higher interest rate ($ ______)		
900. Mortgage Broker Origination Charges† (Line 901 less 902)	$ ______	$ ______
901. Total Broker Compensation for Broker's services $ ______		
902. Amounts paid by Lender to Broker on your behalf ($ ______)		
1000. Credit Report and Pre-Closing Appraisal and Inspection Charges (Appraisal, Credit Report, Tax or Flood Determination, Pre-closing Inspection, Pest Inspection)	$ ______	$ ______
1100. Title and Closing Charges (Sum of lines 1101–1104)	$ ______	$ ______
1101. Title Charges (Lender's Title insurance, Survey, Title examination, Notary services, Abstract or title search, Documentation preparation) $ ______		
1102. Owner's Title Insurance (Coverage $ ______) $ ______		
1103. Closing agent to attend closing† $ ______		
1104. Services required by the closing agent but not by the lender $ ______		
1105. Closing agent services required by Lender† $ ______		
1200. Government Recording and Transfer Charges (Sum of lines 1201–1204)	$ ______	$ ______
1201. Recording fees		
Deed: $ ______ Mortgage: $ ______ Releases: $ ______		
1202 City/county tax stamps Deed. $ ______ Mortgage $ ______		
1203. State tax stamps Deed: $ ______ Mortgage: $ ______		
1204. Other government recording and transfer costs $ ______		
1300. Items Required by Lender to be Paid in Advance (Sum of lines 1301–1306)	$ ______	$ ______
1301. Daily Interest Charges from ______% to ______% at $ ______ per day† $ ______		
1302. Taxes $ ______		
1303. Hazard insurance premium for ______ months at $ ______ per month $ ______		
1304. Flood insurance premium for ______ months at $ ______ per month $ ______		
1305. Mortgage insurance premiums for ______ months at $ ______ per month† $ ______		
1306. Other (specify) ______ $ ______		
1400. Initial Escrow Deposit for escrow account to pay taxes, insurance premiums and other charges (including mortgage insurance premiums† of $ ______)	$ ______	$ ______
1500. Other Mortgage Loan Settlement Charges† required by lender (e.g., life-of loan flood service, wire transfers, lender's attorney's fee life-of loan tax service, other miscellaneous services not shown above)	$ ______	$ ______
1600. Total Mortgage Loan Settlement Charges (Sum of amounts in Columns A and B)	$ ______	$ ______
1700. Net Settlement Charges to be Paid by Borrower at Closing (Line 1600 less 1701 less 1702 less 1703)(also entered on lines 103 and 502)	$ ______	$ ______
1701. Amounts Paid by Borrower before Closing $ ______ (specify item numbers) ______		
1702 Amounts from Lender or Mortgage Broker $ ______		
1703. Settlement Charges Paid by Seller (specify item numbers)	$ ______	

Borrower: compare the amounts for each category (including the amounts the seller has agreed to pay, if any) with the amounts for each category shown on your Good Faith Estimate of Settlement Costs.

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT [Optional language is in brackets] PAGE 3

Combined HUD-1 Statement of Settlement Costs and Final Truth in Lending Act Disclosure

Lender Name and Address	Mortgage Broker Name and Address
Buyer/Borrower Name and Address	**Property Address**

Annual Percentage Rate	Finance Charge	Amount Financed	Total of Payments
The cost of your loan as a yearly rate including interest as shown in the schedule below and other finance charges	The dollar amount the loan will cost you including Prepaid Finance Charges shown on page 2	Your Loan Amount less the Prepaid Finance Charges shown on page 2	The amount you will have paid after you have made all payments as scheduled
________ %	$ ________	$ ________	$ ________

Schedule of Interest Rates, Balances and Payments. Your loan has a term of ________ years, repayable as follows:

Interest Rate	Beginning Principal Balance	Number of Payments	Amount of Payment	Payments Due Monthly Beginning

Payment Increases. If checked below, your loan has features that may cause your payments to increase. Consider carefully whether you can afford to make the higher payments. Do not assume that you will be able to refinance to lower your payments.

☐ **Adjustable Rate:** Your loan contains an adjustable rate feature. See the Truth in Lending Act disclosures provided to you earlier about your adjustable rate feature. If the index used to adjust your interest rate increases, your actual interest rates and payments may be higher than shown above, but your interest rate will not increase above ________ % and your payments will not increase above $ ________

☐ **Interest Only:** The initial monthly payments cover only the interest on your loan amount. If you pay only interest due, after a certain period of time, your monthly payment will increase because you must pay back principal and interest.

☐ **Negative Amortization:** You may be allowed to make payments on your loan that do not cover all of the interest owed. Unpaid interest owed will be added to your principal balance, increasing the amount that you must repay, but your principal balance will not increase above $ ________

☐ **Balloon Payment:** Your loan must be paid off in one large final payoff payment of up to $ ________ after ________ years

☐ **Demand Feature:** The entire amount owed on this loan is payable on demand. This means that the lender may require you to pay off your loan in full at any time. All disclosures are based on an assumed maturity of one year

Mortgage Insurance.

☐ **You will be required** to pay the cost of mortgage insurance for your loan. Any amounts you paid at or before closing are disclosed on page 2 and any costs you will pay after closing are included in the payments shown above

☐ **You will not be required** to pay mortgage insurance for your loan.

Payments for Taxes and Insurance. The payments shown above do not include amounts you will pay for real estate taxes and hazard insurance, estimated to be an additional $ ________ per month. This amount is subject to change throughout the term of the loan.

☐ **Your loan provides** for an escrow account from which the lender will pay your taxes and insurance. Page 2 shows your initial escrow deposit. Monthly escrow payments will be required. You will receive an escrow account statement no later than 45 days after settlement.

☐ **Your loan does not provide** for an escrow account. You are responsible for paying taxes and insurance when due.

Prepayment.

☐ **Your loan has a prepayment charge.** If you pay off during the first [time period], you may have to pay a charge of up to $ ________

☐ **Your loan has no prepayment charge.** If you pay off early, you will not have to pay a prepayment charge

Hazard and Flood Insurance. You may obtain the required insurance from anyone you want that is acceptable to the lender

Late Charge. If a payment is late, you will be charged $ ________

Security. If you obtain this loan, the lender will have a mortgage on your home. You could lose your home, and any money you have put into it, if you do not meet your obligations under the mortgage. You are not required to obtain this loan merely because you have received these disclosures or have signed a loan application.

Assumption. Someone buying your house

☐ **may, subject to conditions, be allowed** to assume the remainder of your mortgage on the original terms

☐ **will not be allowed** to assume the remainder of your mortgage on the original terms.

Borrower Signature　Date　Borrower Signature　Date

Nov 06 08 04:12p Pulte Mortgage, LLC 303-409-5363 p.13

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT [Optional language is in brackets] PAGE 1

Good Faith Estimate of Settlement Costs

Lender Name and Address	Mortgage Broker Name and Address	File Number
Buyer/Borrower Name and Address	Property Address	Date GFE Provided

Loan Description

Proposed Mortgage Loan Amount $______ ☐ Conventional ☐ FHA ☐ VA ☐ FSA/RHS

About this Good Faith Estimate of Settlement Costs

This disclosure contains a Good Faith Estimate of your settlement costs on page 1. These are estimates based on information you provided. If your loan is approved, the estimated amounts may change based upon conditions discovered by the Lender in underwriting, or, if, among other things, you request a change in the loan amount, term, type of loan or lock your interest rate at a different time or on different terms.

Mortgage Loan Settlement Charges to Be Paid by You

The line numbers below correspond to the item numbers on the HUD-1 Settlement Statement you will receive at loan closing. You should compare this Disclosure with the HUD-1 Statement you receive at closing to determine whether any changes have occurred and the reason for any changes. Call your lender or mortgage broker with any questions.

Prepaid Finance Charges of $______ are included in the Settlement Charges shown below and are marked with an †. Your Prepaid Finance Charges together with interest and other lender-required loan related charges you will pay after closing (such as mortgage insurance premiums, if applicable) are shown on your Truth in Lending Disclosure as the Finance Charge.

800. Lender Origination Charges† (Line 801 plus 802 plus 803 less 804) $______

- **801 Lender Charges** for loan origination and other Lender services $______
- **802 Discount Points** paid to reduce your interest rate ______% $______
- **803 Rate Lock** paid to lock in your interest rate ______% $______
  (If you lock in your rate at a different time or on different terms, the lock fee may change. See your Rate Lock Agreement for additional details.)
- **804 Lender Credit** for your choosing a higher interest rate ($______)

900. Mortgage Broker Origination Charges† (Line 901 less 902) $______

- **901 Total Broker Compensation** for Broker's services $______
- **902 Amounts Paid by Lender** to Broker on your behalf ($______)

Important Information When Using a Mortgage Broker. If you have agreed that the Lender may pay the Broker on your behalf part of the Total Broker Compensation (line 902), you will pay this amount through your loan's interest rate and monthly payment. Your Mortgage Broker is required to enter into a Mortgage Broker Fee Agreement with you, which you should review.

1000. Credit Report and Pre-Closing Appraisal and Inspection Charges $______
For credit reports, appraisals, property valuations, inspections, tax or flood determinations.

1100. Title and Closing Charges (Sum of lines 1101–1105) $______

- **1101 Title Charges** $______
  (Lender's title insurance, survey, title examination, notary services, abstract or title search, documentation preparation)
- **1102 Owner's Title Insurance** with title coverage of $______ $______
- **1103 Closing Agent** to attend closing† $______
- **1104 Services Required** by closing agent but not by Lender $______
- **1105 Closing Agent Services** required by Lender† $______

1200. Government Recording & Transfer Charges $______

1300. Items Required by Lender to be Paid in Advance (Sum of lines 1301–1306) $______

- **1301 Daily Interest Charges†** from the day of your settlement until the first day of your normal payment cycle, estimated at $______ per day for 30 days $______
- **1302 Taxes** $______
- **1303 Hazard Insurance Premium** $______
- **1304 Flood Insurance Premium** $______
- **1305 Mortgage Insurance Premium†** $______
- **1306 Other [Specify]** ______ $______

1400. Initial Escrow Deposit† for escrow account to pay taxes, insurance, and other charges $______

☐ Mortgage insurance premium reserves of $______ are included in this amount

1500. Other Mortgage Loan Settlement Charges† such as life-of-loan flood and tax services, lender's attorney's fees, wire transfer and other miscellaneous services not covered above $______

1600. Total Estimated Mortgage Loan Settlement Charges $______

1700. Mortgage Loan Settlement Charges to be Paid by Borrower at Settlements $______
(Line 1600 less 1701 less 1702 less 1703)

- **1701 Amounts Paid by Borrower Before Closing** ($______)
- **1702 Amounts from Lender or Mortgage Broker** ($______)
- **1703 Settlement Charges Paid by Seller** ($______)

Note: In a purchase transaction the amount you will pay at settlement will be affected by whether the seller has agreed to pay any of the settlement charges, by the amount of your down payment, and by the amount you have already paid as a deposit. Settlement charges paid by seller (line 1703) will appear on the HUD-1 Settlement Statement.

You are entitled to shop for a limited number of settlement services. Check with your lender about the services you may shop for. Those services and their charges are included in your Mortgage Loan Settlement Charges shown on line 1700 above; if you shop for these services, however, these amounts may change.

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HUD-1 Statement of Settlement Costs

Lender Name and Address		**Mortgage Broker Name and Address**	
Buyer/Borrower Name and Address		**Seller Name and Address**	
Settlement Agent		**Property Address**	
Settlement Date	**Loan Number**	**File Number**	**MI Number**

Loan Description

Proposed Mortgage Loan Amount $ ____________ ☐ Conventional ☐ FHA ☐ VA ☐ FSA/RHS

About this HUD-1 Statement of Settlement Costs

This disclosure contains a summary of the borrower's and seller's transaction on page 1 and your settlement costs on page 2. You can compare the estimated settlement costs on your Combined Good Faith Estimate of Settlement Costs and Truth in Lending Act Disclosure provided to you earlier to the final settlement costs on page 2.

A. Summary of Borrower's Transaction	B. Summary of Seller's Transaction
100. Gross Amount Due from Borrower	**400. Gross Amount Due to Seller**
101. Contract Sales Price	401. Contract sales price
102. Personal Property	402. Personal property
103. Net Settlement Charges to be Paid by Borrower (line 1700)	403.
104.	404.
105.	405.
Adjustments for items paid by seller in advance	**Adjustments for items paid by seller in advance**
106. City/town Taxes to	406. City/town taxes to
107. County Taxes to	407. County Taxes to
108. Assessments to	408. Assessments to
109.	409.
110.	410.
111.	411.
112.	412.
120. Gross Amount Due from Borrower	**420. Gross Amount Due to Seller**
200. Amounts Paid by or on behalf of Borrower	**500. Reduction in Amount Due to Seller**
201. Deposit or earnest money	501. Excess deposit (see instructions)
202. Principal amount of new loan(s)	502. Net Settlement Charges to be Paid by Seller (line 1700)
203. Existing loan(s) taken subject to	503. Existing loan(s) taken subject to
204.	504. Payoff of first mortgage loan
205.	505. Payoff of second mortgage loan
206.	506.
207.	507.
208.	508.
209.	509.
Adjustments for items unpaid by seller	**Adjustments for items unpaid by seller**
210. City/town taxes to	510. City/town taxes to
211. County taxes to	511. County taxes to
212. Assessments to	512. Assessments to
213.	513.
214.	514.
215.	515.
216.	516.
217.	517.
218.	518.
219.	519.
220. Total Paid By/For Borrower	**520. Total Reduction Amount Due Seller**
300. Cash at Settlement From/To Borrower	**600. Cash at Settlement To/From Seller**
301. Gross Amount Due from Borrower (line 120)	**601. Gross Amount Due to Seller (line 420)**
302. Less Amounts paid By/For Borrower (line 220)	602. Less Reductions in Amount Due Seller (line 520)
303. Cash ☐ From ☐ To Borrower	603. Cash ☐ To ☐ From Seller

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT [Optional language is in brackets] PAGE 2

HUD-1 Statement of Settlement Costs

Lender Name and Address	Mortgage Broker Name and Address
Buyer/Borrower Name and Address	**Property Address**

C. Settlement Charges

Note: Prepaid Finance Charges of $______ are included in the Settlement Charges shown below and are marked with an †. Your Prepaid Finance Charges together with interest and other lender-required loan related charges you will pay after closing (such as mortgage insurance premiums if applicable) are shown on your Truth in Lending Disclosure as the Finance Charge.

C-1. Real Estate Sale Settlement Charges	Column A Paid From Borrower's Funds at Settlement	Column B Paid From Seller's Funds at Settlement
700. Total Real Estate Commission — sales price $______ at ______% A $______		
Division of Commission in 700 is as follows:		
701. $______ to ______		
702. $______ to ______		
703. Real Estate Commission on line 700 paid at settlement	$______	$______
704. Other (specify) ______	$______	$______
C-2. Other Charges for Transactions Not Required by Broker or Lender		
750. Borrower's Attorney's Fee	$______	$______
751. Other (specify) ______	$______	$______
C-3. Mortgage Loan Settlement Charges to Be Paid by You		
800. Lender Origination Charges† (Line 801 plus 802 plus 803 less 804)	$______	$______
801. Lender Charges for loan origination and other Lender services $______		
802. Discount Points paid to reduce your interest rate ______% / $______		
803. Rate Lock paid to lock in your interest rate ______% / $______		
804. Lender Credit for your choosing a higher interest rate ($______)		
900. Mortgage Broker Origination Charges† (Line 901 less 902)	$______	$______
901. Total Broker Compensation for Broker's services $______		
902. Amounts paid by Lender to Broker on your behalf ($______)		
1000. Credit Report and Pre-Closing Appraisal and Inspection Charges (Appraisal, Credit Report, Tax or Flood Determination, Pre-closing Inspection, Pest Inspection)	$______	$______
1100. Title and Closing Charges (Sum of lines 1101–1104)	$______	$______
1101. Title Charges (Lender's Title insurance, Survey, Title examination, Notary services, Abstract or title search, Documentation preparation) $______		
1102. Owner's Title Insurance (Coverage $______) $______		
1103. Closing agent to attend closing† $______		
1104. Services required by the closing agent but not by the lender $______		
1105. Closing agent services required by Lender† $______		
1200. Government Recording and Transfer Charges (Sum of lines 1201–1204)	$______	$______
1201. Recording fees		
Deed $______ Mortgage: $______ Releases: $______		
1202. City/county tax stamps Deed: $______ Mortgage: $______		
1203. State tax stamps Deed: $______ Mortgage: $______		
1204. Other government recording and transfer costs $______		
1300. Items Required by Lender to be Paid in Advance (Sum of lines 1301–1306)	$______	$______
1301. Daily Interest Charges from ______% to ______% at $______ per day† $______		
1302. Taxes $______		
1303. Hazard insurance premium for ______ months at $______ per month $______		
1304. Flood insurance premium for ______ months at $______ per month $______		
1305. Mortgage insurance premiums for ______ months at $______ per month† $______		
1306. Other (specify) ______ $______		
1400. Initial Escrow Deposit for escrow account to pay taxes, insurance premiums and other charges (including mortgage insurance premiums† of $______)	$______	$______
1500. Other Mortgage Loan Settlement Charges† required by lender (e.g., life-of-loan flood service, wire transfers, lender's attorney's fee, life-of-loan tax service, other miscellaneous services not shown above)	$______	$______
1600. Total Mortgage Loan Settlement Charges (Sum of amounts in Columns A and B)	$______	$______
1700. Net Settlement Charges to be Paid by Borrower at Closing (Line 1600 less 1701 less 1702 less 1703)(also entered on lines 103 and 502)	$______	$______
1701. Amounts Paid by Borrower before Closing $______ (specify item numbers) ______		
1702. Amounts from Lender or Mortgage Broker $______		
1703. Settlement Charges Paid by Seller (specify item numbers)	$______	

Borrower: compare the amounts for each category (including the amounts the seller has agreed to pay, if any) with the amounts for each category shown on your Good Faith Estimate of Settlement Costs.

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